CONFIDENTIAL

CONSTITUENT ASSEMBLY OF INDIA

REPORT

of the

EXPERT COMMITTEE

on the

Financial Provisions of Union Constitution

NEW DELHI: PRINTED BY THE MANAGER
GOVERNMENT OF INDIA PRESS, [illegible]

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CONSTITUENT ASSEMBLY OF INDIA

COUNCIL HOUSE
NEW DELHI,
December 5, 1947

To

THE SECRETARY,
CONSTITUENT ASSEMBLY OF INDIA,
COUNCIL HOUSE,
NEW DELHI.

Expert Committee on Financial Provisions

Sir,

I have the honour to forward herewith the Report of the Expert Committee on Financial Provisions of the Union Constitution for submission to the Hon'ble the President.

I have the honour to be,
Sir,
Your most obedient servant,
M. V. RANGACHARI,
Member-Secretary.

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REPORT

Terms of Reference

We were appointed by the President of the Constituent Assembly to examine and report on the Financial Provisions of the Constitution Act with the following terms of reference:—

I. To examine, with the aid of the memoranda on the distribution of revenue between the Centre and the Provinces sent by the Government of India and the Provinces, the existing provisions relating to finance and borrowing powers in the Government of India Act, 1935, and their working during the last ten years and to make recommendations as to the entries in the lists and sections to be embodied in the new Constitution.

The following points shall, in particular, be kept in view in making the recommendations:—

(a) How are taxes to be allocated between the Centre and the Units as regards legislation, levy and collection?

(b) Which are the Federal taxes—

(i) whose net proceeds are to be retained entirely by the Centre;

(ii) whose net proceeds are to be entirely made over to Units;

(iii) whose net proceeds are to be shared between the Centre and the Units?

(c) On what principles the taxes mentioned in (b)(iii) are to be shared between the Centre and the Units?

(d) What is to be the machinery for determining the shares: e.g., whether a Financial Commission should be appointed immediately after the enactment of the Constitution to report on the principles of sharing and their application to be brought into effect when the Constitution comes into force; and whether the same or a similar Commission should review these principles and their concrete application periodically, say, once in five years?

II. What should be the principles on which Federal grants should be made to the Units in future? What should be the machinery for the determination of such grants; could the same Financial Commission as is referred to in I(d) above act as the machinery for this purpose also, or should it be a different one?

III. How could the Indian States be fitted into this general system as far as possible on the same terms as Provinces? Should a time lag be provided for their being so fitted in?

IV. On the assumption of financial responsibility for Defence, Foreign Affairs and Communications on behalf of the Indian States under arrangements for accession to the Federation, what special financial arrangements, if any, are necessary between the acceding States and the Federation?

V. Should the existing rights of the Indian States as to Federal taxes now levied by them be acquired on payment of compensation?

VI. How far is it feasible, on the centralization of all customs levied at the Federal frontiers, to permit Indian States affected by such centralization to retain such portion of the customs so levied at their frontiers as might be attributed to consumption in the States, etc.? [A review of the existing agreements between the Centre and certain important Indian States as regards maritime customs, excises etc. may be of value in this connection.]

VII. Some Provinces have claimed a larger percentage of the income-tax to be made over to them than under the existing system. Does this claim merit consideration; if so, to what extent?

VIII. A suggestion has been made that the Centre should be allocated only the excises on specified commodities, the rest of the field of excise being left to the Provinces to tap according to their needs. Would this be possible without any material detriment to Federal revenue?

IX. On the basis that the residuary powers are vested in the Centre in the new Constitution so far as the Provinces are concerned, and in the States so far as the States are concerned, is it necessary that any additional specific taxes should be entered in the Provincial List, and if so, what?

X. Is it necessary to make any modifications in the existing provisions as regards procedure in financial matters contained in Sections 36 to 37 and 78 to 83 of the Government of India Act, 1935?

XI. A large number of Indian States at present derive substantial revenues from land customs levied at the frontiers between their limits and those of neighbouring States or Provinces. One of the fundamental rights already adopted by the Constituent Assembly is to remove all internal barriers in regard to trade between Unit and Unit. Could these land customs be done away with either immediately or over a period of years, and if so, should any prejudice caused thereby to the finances of particular States be compensated and in what manner?

[The Committee should kindly indicate clearly which of its recommendations should go into the body of the Constitution and which should be provided for by Federal law.]

Prefatory Remarks.

2. We began our work on the 17th November and have been sitting continuously. We have received memoranda from the various Provincial Governments setting out their claims for larger resources as well as their points of view in connection therewith. We have also received a memorandum from the Ministry of Finance of the Central Government giving a picture of the financial position of the Centre in the near future. The Secretariat of the Constituent Assembly has collected for us information on various matters relating to the States, and also helpful information regarding other Federations. It has also prepared a draft of the sections which come within our terms of reference; and this has considerably helped us in our work. We are indebted for all these memoranda, information and drafts. We are also indebted to some of the Provincial authorities who appeared before us in person and discussed with us informally the questions arising out of the memoranda presented by their Governments. We availed ourselves also of the specialised knowledge and experience of not only some of the officials of the Central Secretariat, but of some members of the Constituent Assembly and others who have unique knowledge of some of the problems under our consideration. All our discussions, however, were free and informal; and we did not, therefore, record any evidence, apart from the memoranda placed before us.

3. In particular, the other two of us would like to place on record our grateful appreciation of the assistance we have received from our colleague and Secretary Mr. Rangachari, who amidst his exacting, multifarious duties, including the preparation of the interim budget not only found time regularly to attend our meetings, but also placed his wide knowledge and experience at our disposal, and arranged to secure at short notice most of the available information required by us. We should also like to thank Mr. B. Das Gupta of the West Bengal Government Secretariat for the intelligent and extremely well informed assistance

he gave us. We are also indebted to Mr. Mukerjee, Joint Secretary of the Constituent Assembly, for his help throughout our sittings and in particular for putting our recommendations in the shape of draft amendments to the Constitution.

4. Our terms of reference may be divided broadly into the four following groups:

(1) Relations between the Centre and the Units, and between the Units *inter se;*

(2) Financial procedure, *i.e.*, relating to the budget, expenditure and money Bills;

(3) Borrowing powers of Units; and

(4) Relations of the Union with the States.

We have accordingly, for convenience, regrouped our terms of reference as follows.

(1) I, VII, VIII, IX, II

(2) X

(3) I

(4) III, IV, V, VI, XI

and discussed them as far as possible, in the above order.

Brief History of Financial Relations

5. Before dealing with the working of the financial arrangements in the Government of India Act, 1935, it is necessary to give a brief account of the earlier arrangements so that we can have a correct picture of the problems before us.

6. The period before the passing of the Government of India Act, 1935, falls into two well-defined parts, namely, the period ending with the 31st March, 1921, *i.e.*, before the operation of the Government of India Act, 1919, and the period covered by that Act.

7. The process of financial development in this country has been one of evolution from a unitary to a quasi-federal type. The Government of India started as a completely unitary Government in entire control of the revenues of the country with the Provincial Governments depending on the Central Government for all their requirements. In the earlier years, Provincial Governments were given fixed grants for meeting the expenditure on specific services, and the first step in making specific sources available to them was taken when the Provincial Governments were given the whole or part of certain heads of revenue like Forest, Excise, Licence Fees (later to develope into Income-tax), Stamps, Registration, Provincial Rates, Law and Justice Public Works, Education etc. The funds released by this allocation were not adequate for the requirements of the Provinces and had to be supplemented, mainly by sharing with them in varying proportions the main source of Central revenue, namely, Land Revenue, and partly by making to them additional cash assignments. In 1904, the settlements with the Provinces were made quasi-permanent, thereby making the Provinces less dependent on the fluctuating grants from the Centre. This method of financing the Provinces was examined more than once and retained as the best suited to the then circumstances.

8. The Government of India Act, 1919, which, among other things, aimed at giving a reasonable measure of autonomy to the Provinces as the first step in the process of self-government, made the first clear-cut allocation of resources between the Centre and the Provinces without having any divided heads between them. Under this Act, certain specific heads were given wholly to the

Provinces and the remaining sources were retained by the Centre. Thus among the principal heads of revenue, Land Revenue, Excise and Stamps were given to the Provinces, while the Centre retained Customs, Income-tax, Salt and Opium the three great Commercial departments of Government, Railways and Posts d Telegraphs were retained by the Centre, while irrigation was handed over to the Provinces.

9. This allocation of resources between the Centre and the Units, particularly e assignment of the whole of Land Revenue to the Provinces, left the Central budget in a substantial deficit; and in the earlier years of this scheme, the Centre had to depend on the Provinces for contributions for balancing its budget. These contributions were fixed by what is commonly known as the Meston Award, and were designed to produce for the Centre an estimated shortfall of Rs. 9·8 crores resulting from the rearrangement of resources between the Centre and the Provinces. The contributions ranged from Rs. 348 lakhs from Madras to Rs. 15 lakhs from Assam, while one Province, namely, Bihar and Orissa, had to make no contribution at all. It is unnecessary for the present purpose to describe in detail the method by which these contributions were fixed. It is enough to mention that they became a source of constant friction between the Centre and the Provinces; and when substantial Provincial deficits occurred, an unceasing clamour developed for their withdrawal Between 1925 and 1928 these contributions were partially remitted and they were completely extinguished in 1929.

10. The experience of the years under the 1919 Act clearly showed that the sources of revenue allocated to the Provinces were inelastic, and were insufficient to meet the increasing requirements of the Provinces for their expanding needs for nation building services such as Education, Medical Relief, Public Health etc., which fell almost wholly in the Provincial field It was clear that some additional revenue heads had to be released to the Provinces; and while the Government of India Act, 1935, did not make any radical change in the allocation of heads between the Centre and the Units, it revived in a somewhat modified form the earlier principle of dividing the proceeds of certain Central heads, the two heads concerned being Customs and Taxes on Income The Act also provided for the grant of fixed subventions to some of the smaller Provinces, and gave the Centre power to raise Excise and Export duties for distribution among the Provinces and federating States. After an enquiry into the relative needs of the Centre and the Provinces by Sir Otto Niemeyer, the Provincial shares in the divided heads of Central revenue and the subventions to some of the Provinces were fixed by an Order-in-Council, which, subject to a modification during the war, continued till 15th August, 1947

Present Constitutional Position

11. Under the Government of India Act, 1935, which is the starting point of our enquiry, the taxing jurisdictions of the Central and Provincial Legislatures are entirely separate. But, while the Provinces retain the whole of the net proceeds of all taxes levied by them, the Central Government has to give away either in part or in whole the net proceeds of some of the taxes levied by it.

12. The taxes, the net proceeds of which are to be given away wholly to the Provinces, if levied, are—

(1) Federal Estate and Succession duties,

(2) Federal Stamp duties,

(3) Terminal Taxes on goods and passengers carried by Railway or Air;

(4) Taxes on Railway fares and freights.

The Centre can levy a surcharge on those taxes entirely for its own purpose. None of these taxes has in fact been levied, except that the Federal Stamp duties continue to be levied under the old laws, the duties however being collected and retained by the Provinces.

13. The Federal Taxes, the net proceeds of which are to be shared with the Provinces, fall into two groups :—

(1) taxes, the sharing of the net proceeds of which has been made obligatory by the Constitution *viz.*, income-tax and jute export duty;

(2) taxes, the sharing of the net proceeds of which has been left to be determined by the Federal Legislature *viz.*, Central Excises including duty on salt, and export duties except on jute and jute products. The Central Legislature has levied certain taxes under these heads, but has not provided for giving any share to the Provinces.

14. Besides providing for giving away the net proceeds of taxes in whole or in part to the Provinces, the Constitution also provides for fixed grants-in-aid to some Provinces.

15. There is also a general provision for giving grants to Provinces at the discretion of the Central Government either for general or specific purposes.

16. Two tables showing the Constitutional position in respect of the revenues of the Federal and Provincial Governments respectively under the Government of India Act, 1935, will be found in Appendix I. We are indebted to Mr. Ayyangar's commentary on the Government of India Act, 1935, for these tables.

Review of Finances of Provinces and the Centre.

17. Two tables giving the financial position of the Provinces and the Centre during the years 1937-38 to 1946-47 are set out in Appendix II. In considering the working of the existing arrangements during the last decade, the most important point to note is that war broke out soon after the Government of India Act, 1935, came into operation.

18. During the war, all Provinces except Bengal and Assam had surplus budgets. Revenue receipts increased several times, mainly on account of war-time conditions and also because the Provinces levied a number of new taxes and increased the rates of existing ones; there were remarkable increases in receipts under Provincial, i.e., Liquor and Drugs, Excises, and in the Provincial share of Income-tax. Most Provinces were under Section 93 administration. All development work was stopped. The Provinces are now faced with a heavy programme of expenditure without any corresponding increase in revenue. On the contrary, even apart from voluntary abandonment of revenue as in the case of Liquor Excises, the revenue is likely to go down much below wartime levels. Land revenue, both in the permanently and temporarily settled provinces, is not likely to expand. State purchase of zamindaries will not bring any return for years to come In ryotwari Provinces, remissions are likely to be more liberal than before, and there is thus little prospect of an increase in land revenue. Receipts from stamps and registration fees are not likely to increase much, while forest revenue will perhaps dwindle on account of large scale felling during the war Receipts from sales tax, electricity tax and entertainment tax may not fall, though they will be below the war-time peak for some time to come.

19. During the war and after, most of the Provincial Governments have practically exhausted the entire field of taxation reserved for them. Moreover, Provincial Governments have to share the Provincial field with Local Bodies, and on that account too, need adequate resources. A substantial transfer of revenues from the Centre to the Provinces, therefore, seems inevitable, if essential and overdue programmes of social service and economic development have to be undertaken.

20. At this stage, we would refer to the adoption, by most Provincial Governments, of a prohibitionist policy; and of the inevitable loss of substantial revenue by all of them. Obviously, it is for the provinces to find alternative provincial resources from which to recoup the loss; and in any case, it would not be practicable for provinces to expect sufficient assistance from the Centre for this purpose, at any rate for many years. The point that we wish to emphasise is that it will be for the Provincial Governments to balance the urgency of schemes of development against the advisability of social reforms like prohibition, and that in any case, they must not embark on schemes, whether of reform or development, depending merely on the possibility of obtaining assistance automatically from the Centre.

21. To turn now to the Centre, it has been working on deficit budgets. The large surpluses that were expected sometime ago have not been, and are not likely to be, realised, mainly because of the food shortage, the refugee problem and other causes arising out of the partition of the country, particularly, continued heavy expenditure on Defence. These are, however, temporary problems, and we consider that the financial position of the Centre is essentially sound. As these temporary problems are solved, the budgetary position of the Centre will necessarily get better. There is scope for improvement in the administration of Central taxes, and particularly of taxes on income. In respect of taxes on income, it should be possible for the Centre not only to collect more in future in the ordinary course every year but to secure for the exchequer, by legislative changes, if necessary, the large sums that are believed to have been successfully kept back from the Government in recent years. We do not, however, expect any appreciable change under Customs and Excise; and we do not expect Railway contributions on anything like the scale during the war. Even after the temporary problems referred to above have been solved, expenditure on Defence and Foreign Affairs would still be substantial. The Defence Services will probably be reorganised and re-equipped, and it is not possible to foresee what would be the scale of expenditure for properly equipped defence services even on a peace-time basis. There is little prospect on the other hand of reduction in the service of the national debt but there is, however, scope for reduction in the existing civil expenditure.

22. The problem before us is how to transfer from the Centre to the Provinces, sufficient amount which, while not placing too great a strain on the Centre, would provide adequate resources for the inauguration of useful schemes of welfare and development by the Provinces. While the Centre, on its present basis, may not be in a position to part with substantial sums, we feel that with the resolution of its temporary difficulties and improvement in its tax administration, together with the levy and collection of taxes evaded in the past, it can with no serious risk to its own budget part with sizable sums every year. We are suggesting later in detail how these sums should be regulated. We have already referred to the need for Provinces having clear priorities as between contending demands for money, and we have no doubt that the Provinces will in the earlier years utilise the additional resources now placed at their disposal by concentrating on schemes that would add to the productive capacity of the country and consequently the income of the people and thus enable the provinces to embark on further schemes of reform and development.

Claims of Provinces

23. Every Province has drawn pointed attention to the urgency of its programmes of social service and economic development and to the limited nature of its own resources, both existing and potential, and all of them have asked for substantial transfer of revenues from the Central sources. A summary of the detailed suggestions made by them, which very considerably, is set out in Appendix III.

24. On the question of apportionment of income-tax among Provinces also, the provinces differ widely in their views. Bombay and West Bengal support the basis of collection or residence, the United Provinces that of population, and Bihar a combined basis of population and orgin (place of accrual); Orissa and Assam want weightage for backwardness. East Punjab, while suggesting no basis, wants her deficit of Rs. 3 crores somehow to be met.

25. In the case of excise taxes, the bases suggested are production, collection, consumption and population, while Assam suggests some weightage for its low level of revenue and expenditure. Assam has further pressed for special treatment of excises collected on wasting assets, e.g., the petroleum raised in Assam. Assam also wants a share of the export duty on tea.

General Observations

26. Before we proceed further we would make a few general observations.

India has a federal form of Government, and every federation is based on a division of authority and involves a certain amount of compromise. In this country, federation has been the result of gradual devolution of authority. It has not come into existence through agreements among sovereign States as in some other federations.

27. What we have to do is to distribute the total available resources among Federal and Provincial Governments in adequate relation to the functions imposed on each; so, however, that the arrangements are not only equitable in themselves and in the interests of the country as a whole but are also administratively feasible. We have also to ensure that there is not too violent a departure from the *status quo*, and also to see that while we have as much uniformity as possible, weak Units are helped at least to maintain certain minimum standards of services.

28. The basic functions of a Federal Government are Defence, Foreign Affairs and the service of the bulk of the national debt, and they are all expensive functions, particularly in the light of the limited resources of the country. The head "Communications" would ordinarily at least pay for itself. The Federal Government may also have to assume leadership in the co-ordination and development of research and higher technical education. Normally, however apart from war or large scale internal disorder, the expenditure of the Centre should be comparatively stable. The needs of the Provinces are in contrast, almost unlimited, particularly in relation to welfare services and general development. If these services, on which the improvement of human well-being and increase of the country's productive capacity so much depend, are to be properly planned and executed, it is necessary to place at the disposal of Provincial Governments adequate resources of their own, without their having to depend on the variable munificence or affluence of the Centre. The Provinces must, therefore, have as many independent sources of revenue as possible. On the other hand, it is not practicable to augment their revenues to any considerable extent by adding more subjects to the Provincial Legislative List, without simultaneously upsetting the equilibrium of the Centre. We cannot, therefore, avoid divided heads; and what we have to aim at is to have only a few divided heads, well balanced and high-yielding, and to arrange that the shares of the Centre and the Provinces in these heads are adjusted automatically without friction or mutual interference.

29. In this country the lack of sufficient economic and financial statistics and other similar data is a great handicap. Therefore, the allocation of resources has to be made largely on the basis of a broad judgment, at any rate until the necessary data become available. We attach great importance to the collection of these statistics and to connected research, and trust that the Government will make the necessary arrangements without delay. In the meantime we have made our recommendations on the best judgment we could give to the exiguous data available.

Lists of taxes for the Centre and the Units

30. We recommend no major change in the list of taxes in the Federal Legislative List as recommended by the Union Powers Committee. We, however, recommend the substitution of the limit of Rs. 250 for Rs. 50 in clause 200 of the Draft Constitution relating to taxes on professions, trades, callings and employments. We observe from the Draft Constitution that it has been proposed to transfer to the Federal Legislative List stamp duty on transfer of shares and debentures, but we presume that the duties will continue to accrue to the Provinces. In view of the far-reaching effects on public credit and finance of Stock Exchange transactions, we consider that the Centre should have the power to legislate for the regulation of such transactions. If such regulation involves the levy of taxes, we recommend that such taxes should be retained by the Centre except that if the taxes take the form of mere duties on transfers of shares and debentures, the Provinces should have these duties just like other Stamp duties. We accordingly recommend the entry in the Federal Legislative List of a new item "Stock Exchanges and futures market and taxes other than Stamp duties on transactions in them"

31. In the list of taxes in the Provincial Legislative List, we recommend the following changes:—

(1) In entry 43, the words "hearths and windows" may be deleted. Such taxes are not likely to be levied. In any case, they would be covered by the word "buildings"

(2) In entry 53, the word "cesses" should, we think, be replaced by the word taxes'

(3) Similarly, in entry 56, we would substitute the word "taxes" for the word dues'

(4) In entry 50, we would make the following changes:—

(a) for the word "sale", we would substitute "sale, turnover or purchase' in order to avoid doubt.

(b) We would also add words such as "including taxes in lieu thereof on the use or consumption within the Province, of goods liable to taxes by the Province on sale, turnover or purchase". This addition is suggested in order to prevent avoidance by importing for personal use from outside the province.

32. One of the Provincial Memoranda has suggested that the entry "State Lotteries" should be transferred to the Provincial List, but, as we do not wish to encourage State Lotteries, we should prefer the subject to remain Central where, too, we hope, it will not be used.

Shares in certain taxes

33. We have no new items to suggest for insertion in the Provincial Legislative List.

34. The Federal Government will levy and collect all the taxes in the Federal Legislative List. But, according to our recommendations in the following paragraphs the Centre will retain the whole of the net proceeds of the following taxes only, viz.:—

(1) Duties of customs, including export duties.

(2) Taxes on capital value of assets and taxes on the capital of Companies.

(3) Taxes on Railway fares and freights.

35. At present, the Central Government shares the net proceeds of the Jute Export duties with the jute-growing Provinces and has to hand over to the

Provinces the whole of the net proceeds of taxes on railway fares and freights, if levied. As regards the latter, we recommend that, if such taxes are to be levied at all, they should be wholly Central, for, we cannot see any difference in substance between such taxes and a straight addition to fares and freights. As regards the former we are of the opinion that an export duties are capable of very limited application and have to be levied with great caution, they are unsuitable for sharing with the Provinces.

36. It is necessary, however, to compensate the Provinces concerned for the loss of this item of revenue, and we recommend that, for a period of 10 years or till the export duties on jute and jute products are abolished, whichever may be earlier, fixed sums as set out below be paid to these Governments as compensation every year.

Province	*Amount*
	Rs.
West Bengal	100 lakhs.
Assam	15 ,,
Bihar	17 ,,
Orissa	3 ,,

In arriving at these figures which we have based on the figures of pre-war years, we have taken all relevant circumstances into account, and in particular the concentration of manufacture in West Bengal. If at the end of ten years, which we think should be sufficient to enable the Provinces to develop their resources adequately, the Provinces still need assistance in order to make up for this loss of revenue, it would no doubt be open to them to seek grants-in-aid from the Centre, which would be considered on their merits in the usual course by the Finance Commission.

37. Of the remaining Federal Taxes, we recommend that the net proceeds should be wholly or partly given away to the Provinces as indicated below:

38. **Taxes on Income.**—Under the present arrangement the Provinces receive 50 per cent. of the net proceeds of income-tax, except what is attributable to Chief Commissioners' Provinces and taxes on federal emoluments. The net proceeds of the Corporation Tax are also excluded for the purpose of the sharing. Subject to what we have said in paragraph 49 regarding tax on agricultural income, we recommend that, while the net proceeds attributable to Chief Commissioners' Provinces should be retained wholly by the Centre, the other reservations should go, and that the Provinces should get not less than 60 per cent. of the net proceeds of all income-tax including the net proceeds of Corporation Tax, and taxes on federal emoluments. For the purpose of the division, income-tax will mean any levy made under the authority of the entry "Taxes on Income" in the Federal Legislative List

39. We also consider that over and above its share in the net proceeds retained by it normally, the Centre should be empowered to levy a surcharge whenever conditions require such a levy; obviously such occasions should be rare and not last for unduly long periods

40 **Central Excise Duties.**—Excise duties are ordinarily closely connected with customs duties and, barring liquor and drug excises, which we consider, should continue to remain Provincial, are inherently not suited for provincial taxation. On the other hand, they are only a species of consumption taxes of which another species namely, sales, turnover and purchase taxes have been the subject of provincial taxation for some time. The Memoranda received by us from the Provincial Governments are almost unanimous in demanding some share under excises; and our problem is to find not only more resources for the units but to make their revenues more

balanced. If it was possible to have excises on commodities not subject to Customs duties (whether revenue or protective) or not competing, or capable of competing with, or of substitution for, commodities subject to customs duties, e.g., on rice or wheat or millets or on jute and jute goods consumed in India, we see no reason why such excises or a share thereof should not be allotted to the units, apart from the general political objection to the division of heads viz., the divorce of benefit from responsibility. But such excises are not likely to be levied. Again, it is obvious that Excise duties on commodities subject to a protective tariff or even a high revenue tariff could not be conveniently shared. In the circumstances, the utmost that we can suggest by way of assistance in this respect to the Provincial Governments is to hand over to them a share of one of the important Central Excises on a commodity not receiving tariff protection viz., Tobacco. Incidentally, the effective administration of this excise requires the active co-operation of Provincial Governments, which would be better forthcoming if they had a share in the tax. We are averse to giving the units a share in too many Central Excises; for, such an arrangement would not only magnify the political objection of benefit without responsibility but lead to administrative inconvenience, since the rates could not be altered except by the consent of all the beneficiaries.

We accordingly recommend that 50 per cent. of the net proceeds of the excise duty on tobacco should not form part of the revenues of the Federation but should be distributed to the Provinces.

41. It will be seen from what has been said above that we are not in favour of the suggestion made in item VIII of the Terms of Reference viz., that the Centre should be allocated only the excises on specified commodities, the rest of the field of excise being left to the Provinces.

42. **Estate and Succession Duties.**—These duties cannot be administered satisfactorily except by or in the closest touch with the income-tax staff; and in any case, if the Centre is to part with a substantial amount of taxes on income and also a part of certain Central excises, it is appropriate that it should get a share of the estate and succession duties. This will also give to the Federal Government a direct interest in the duty. Subject to what we have said in paragraph 49 about taxes on agricultural property, we recommend that not more than 40 per cent. of the net proceeds of such duties should be retained by the Centre.

43. **Federal Stamp Duties.**—We recommend the continuance of the *status quo*, i.e., the legislation in respect of the duties on the specified documents should be Central but Provinces will collect and retain the duties.

44. **Terminal Taxes on goods or passengers carried by railway or air.**—These taxes are not suitable except for purely local purposes, i.e., for the benefit of municipalities, pilgrim funds, etc., but they can be conveniently levied and collected only by the Centre. The existing provisions may stand

Grants-in-Aid and Subventions

45 Item II of our terms of reference refers to Grants-in-aid.

Assam and Orissa now get fixed subventions of Rs. 30 and Rs. 40 lakhs per annum, respectively. The recommendations that we have made for the increase in the Provincial share of income-tax and the transfer of a share in the excise on tobacco will increase their revenues substantially like those of other Provinces. Even so, however, we have little doubt that these two Provinces will still require fixed subventions on higher scales than at present.

The position of East Punjab is peculiar. Everything there is unsettled, and it will take some time for things to settle down. It is clear, however, that this Province will require a substantial annual subvention for some time to come.

The position of West Bengal is uncertain, and it is not clear how her finances will shape as a result of the partition The liability that she will have to take over as a result of the partition is not yet known All told, however, she will perhaps need some temporary assistance

46. For lack of time and data, we have not been able to assess the subventions required by these four Provinces. We, therefore, recommend that the Central Government should immediately take up the question so that the amounts required by each of these Provinces may be determined in time The amounts should be subject to periodical review by the Finance Commission to which we refer later.

47. We have suggested elsewhere that till the Finance Commission has been able to recommend a better basis of distribution, a part of the divisible pool of income-tax should be used in order to mitigate hardship in individual cases This provision also contains an element of grants-in-aid.

48. It is clear that during the developmental stages of the country it will be necessary for the Centre to make specific purpose grants to the Provinces from time to time. The provisions of clause 203 of the Draft Constitution seem to be adequate for the purpose. We have considered the question whether, as in Australia, grants should be made in order to equalise, or at any rate to reduce the disparity between the levels of services and of severity of taxation in the different provinces. There is undoubtedly something attractive in seeking to bring up the backward units at least to 'average' standards, both in effort (severity of taxation) and in performance (standards of services). In Australia, the maximum difference between the levels is said to be of the order of 20 per cent. and the number of unit States is small. In India, on the other hand, as for example in the U. S. A., the difference in the levels is very wide and the number of units larger when acceding States come into the picture. In such a background 'averages' would be mere mathematical concepts totally unrelated to actual facts. On the other hand, even in a Federation of autonomous units, there is a great deal to be said for helping the less prosperous units to come up to the level of the more prosperous ones. As in all such matters, we must take a realistic decision with reference to the conditions in our country. While we do not recommend the adoption in this country of the Australian system, we have no doubt that the Centre, when distributing specific purpose grants under clause 203 of the Draft Constitution, will bear in mind the varying circumstances in the different Provinces.

48A. Section 199 of the Draft Constitution provides for special assistance to Assam in respect of expenditure for promoting the welfare of scheduled tribes in the Province. We agree with this provision. It has been represented to us on behalf of Orissa that a similar provision should be made for assisting her to develop the backward areas of the Province. In the absence of any data, we have been unable to assess the measure of assistance, if any, required by this Province, and we content ourselves with expressing the view that if the Central Government, after a due examination of the question in all its aspects, decide that special assistance is necessary it should be provided on adequate scale

Taxes on Agricultural Income and Property

49. It is obvious that the taxation of agricultural income by the Provinces, while all other income is taxed by the Centre, stands in the way of a theoretically sound system of income-tax in the country. We should, therefore, have liked to take this opportunity to do away with this segregation. In view of the ease with which the origin of agricultural income can be traced, it could be arranged that the tax from such income, even though levied and collected by the Centre as part

of an integrated system of income-taxes, should be handed back to the Provinces; and it could be further arranged that till such time as the Centre in fact levied a tax on agricultural income, the Provinces already levying this tax might continue to levy it without restriction and with full power to vary the rates of tax. The interests of Provinces could thus be fully protected, and there could, therefore, be no financial objections from them. On the other hand, the present arrangement has the political merit of keeping together in one place both benefit and responsibility, a rather important point, seeing that the Provinces will have full control over but few important heads of revenue. A few provinces have, in fact, levied the tax and are administering it for some time. Perhaps also, the Provinces can administer this particular tax with greater facility than the Centre. For the present, therefore, we have decided to continue the *status quo*, but, in view of the importance of the matter, would recommend that the Provinces should be consulted at once and if a majority, including of course those now levying the tax, agree, tax on agricultural income may be omitted from the Provincial List of subjects, consequential changes being made elsewhere in the Constitution. Our foregoing remarks apply *mutatis mutandis* to Succession and Estate Duties on agricultural property also.

Division of proceeds of Revenue between Provinces

50. **Income-tax.**—As regards the basis of distributing between Provinces the share of proceeds from taxes on income, we are of the opinion that no single basis would lead to equitable results. Origin or *locus* of income is no doubt relevant, but in the complex industrial and commercial structure of modern times, where a single point of control often regulates a vast net-work of transactions, where the raw materials come from one place, are processed in another, manufactured in a third, marketed wholesale in a fourth and ultimately sold in retail over a large area, contracts are made at places different from where they are performed, money is paid in at one place and goods delivered at another and more than one of these stages relate to the same tax-payer, the assignment of a share of profits to each stage can only be empirical or arbitrary

51. Again, the residence of the tax-payer is an important factor, but apart from the artificial legal definition of residence for income-tax purposes, the predominance of joint stock enterprise in business, the dispersion of the shareholders of companies all over the country and even outside, the possibility (emerging from the artificial definition) of simultaneous residence in more than one area, the non-assessment (due to various reasons) of a large number of shareholders, and the absence of authoritative, i.e., tested, information in the income-tax records as to the province of residence of a resident of India (for, today, it is immaterial to the Income-tax Department in which particular Province an assessee is resident), all these together make this criterion of residence a difficult factor to apply in practice in distributing the proceeds of the tax. Even if the statistical difficulties were got over, residence could be changed at the will of the tax-payer

52. Another possible criterion is the place of collection. This place is usually the principal place of business of the tax-payer, or his residence, if he is not carrying on a business or profession. The objection to this factor is that it is unfair to the areas of origin and sale which it completely ignores, while it gives far too much weight to the place of control of a business, which is usually, though not necessarily, the place of collection. Moreover, even more than in the case of residence, the place of collection can be easily altered at the will of the tax-payer.

53. Another possible basis is that of needs i.e., the shares would be regulated somewhat like grants-in-aid, and rather than go into elaborate enquiries for this purpose, the population of a Province could be taken as a rough measure of its needs. The objection to this basis is that a 'share' is something to which a

Province is entitled because its citizens or things have in some measure contributed to the fund, while a grant is something given to it without regard to its contribution to the Centre or to any common pool.

54. We have said enough to show the difficulties of the problem, but the difficulties have somehow to be faced and met, unless we keep the whole of the taxes on income as Central and permit Provinces simultaneously to levy a Provincial income-tax on the basis of origin. In our opinion the latter course is not feasible in the circumstances of this country even if justifiable in theory, and pending enquiry by the Finance Commission the setting up of which we suggest later, we have no choice except somehow to make the distribution on as equitable a basis as can be devised in the circumstances.

55. We propose to proceed on the basis of collection as well as population and also to make some provision for adjustment on the basis of need. We recommend that the Provincial share i.e., 60 per cent. of the net proceeds be distributed among the Provinces, as follows:—

20 per cent. on the basis of population.

35 per cent. on the basis of collection.

5 per cent. in the manner indicated in paragraph 56.

60

For the distribution of the first two blocks, population figures of the previous census and collection figures as certified by the Auditor-General should be accepted as authoritative.

56. The third block of 5 per cent. should be utilised by the apportioning authority as a balancing factor in order to mitigate any hardship that may arise in the case of particular Provinces as a result of the application of the other two criteria; in distributing this block it would be open to the authority to take into account all relevant factors.

57. **Excise duty on tobacco.**—In our view, the most equitable method of distributing this duty is on the basis of estimated consumption. We have no doubt that the Government will take steps to obtain necessary statistical information if it is not already available.

58. **Estate and Succession Taxes.**—These taxes have not so far been levied. One of the hurdles to be crossed before they can be levied is the determination of the manner of distribution of the net proceeds among Provinces. Until the taxes are actually levied and collected for some time, no data about their incidence will be available. Hence, the levy will have to start with some *a priori* basis of apportionment among Provinces. We accordingly recommend that until the Finance Commission is in a position to evolve a better method on the basis of data available to it, the net proceeds should be distributed among the Provinces as follows:—

The net proceeds attributable to real property—On the basis of the location of the property.

Of the balance—

75 per cent. on the basis of the residence of the deceased

25 per cent. on the basis of the population of the Province.

The administration and distribution of these taxes would, in the ordinary course, fall on the Central Board of Revenue, but it would be necessary to empower an appropriate authority to adjudicate in the case of disputes between Provinces as to the residence of individuals.

Effect of the proposals

59. The net effect of all our recommendations together is that, on the present basis of revenue, the Centre will have to transfer to the Provinces a sum of the order of Rs. 30 crores annually. It will recover a part of this loss by the imposition of the Estate and Succession Duties, of the net proceeds of which it will retain 40 per cent. We believe that it will not be beyond the capacity of the Centre to part with this amount annually during the next five years, though it must cause some strain, while at the same time the transfer will enable the Provinces to start their programme of essential social services and economic development.

60. In our recommendations regarding the distribution of proceeds of taxes among the Provinces, we have not only proceeded on more than one basis, but have provided for an element of flexibility in order to mitigate hardship. We have also provided for a periodical review so that the method of apportionment can be adapted to changing conditions from time to time on the basis of experience. We have further provided for grants-in-aid both to the weaker Provinces and to Provinces in difficulty

61. We have also tried to make the whole arrangement as automatic and free from interference as possible. The basic features of the scheme will be embodied in the Constitution itself, while periodic changes will be made by the President on the recommendation of the Finance Commission, which we hope, will command the confidence of all. As frequent changes are undesirable, we have recommended a five-yearly review, though in special circumstances the Finance Commission may embark on a review at a shorter interval. The Provinces will now be sure of their position and can go ahead with their plans

62. It is needless for us to add that to the extent that the Centre transfers its resources to the Provinces in the shape of new or increased shares in revenue, its ability to give grants to the Provinces for specific or other purposes must be correspondingly reduced.

63. We may not have been able in our proposals to satisfy everybody or to provide for every contingency that may possibly arise in the future, but we have tried to do the best possible under the circumstances.

Finance Commission

64. For reasons already stated, our recommendation as to the initial basis of apportionment among Provinces is not intended to be permanent. Conditions may change. The working of the scheme for some time will in itself produce some data that would indicate the nature and direction of the changes required. It is necessary, therefore, to have a periodical review of the whole position by a neutral expert authority.

65. We recommend for this purpose, among others, the appointment of a high level Tribunal of five members including a Chairman who has been, or is, holding high judicial office, not lower than that of a Judge of a High Court. This Tribunal may be called the 'Finance Commission'. There may not ordinarily be enough work for the Commission to keep it busy continuously, and the members need not, therefore, devote their whole time to the work. The members should be appointed by the President in his discretion if only because a Commission of this kind would have frequently occasion to deal with points of conflict between the Centre and the Units. While we would not lay down any conditions in the Statute as to how these members should be selected, we recommend that two should be selected from a panel of nominees of Unit Governments and two others from a panel of nominees of the Central Government, the Chairman being selected by the President himself. One at least of the five should possess close knowledge of the finances and accounts of Governments, while another at least should have a wide and authoritative knowledge of economics. It would be an advantage if one or more were public men with wide experience. It would be a further advantage

if a member possessed more than one qualification, and steps should be taken to secure the services of such individuals. The appointments might be made for 5 years and be renewable for another five years.

66. Between now and the setting up of the Finance Commission, we recommend that the Central Government should take steps in consultation with the Provinces, to collect, compile and maintain statistical information on certain basic matters such as the value, volume and distribution of production, the distribution of income, the incidence of taxes, both Central and Provincial, the consumption of important commodities, particularly those that are taxed or likely to be taxed, etc. The Finance Commission, when set up, would then have some basic information to go upon, and would no doubt call for such further information as it may need. It would also, to the extent necessary, arrange for continuous examination and research in respect of all important matters.

67. The Finance Commission should be entrusted with the following functions:—

(a) To allocate between the Provinces, the respective shares of the proceeds of taxes that have to be divided between them;

(b) To consider applications for grants-in-aid from Provinces and report thereon;

(c) To consider and report on any other matter referred to it by the President.

68. While these categories would exhaust the duties of the Commission, it should be open to the Commission to make any recommendations it may think expedient in the course of the discharge of these duties. It may, for example, suggest a variation in the heads of revenue assigned to the Provinces, i.e., the transfer of new heads or the withdrawal of existing heads, or increases in the shares of existing heads or a reduction in these shares. In making all such recommendations, the Commission will take into account all relevant matters, including the state of finances of the Centre. Its recommendations, in so far as they do not involve any change in the Constitution, would, when accepted by the President, be given effect to by him by order, while recommendations involving a change in the Constitution, if similarly accepted by him, would be dealt with like any other proposed amendment to the Constitution.

69. The Commission's first function would be of the nature of an arbitration, and therefore, the Commission's decisions will be final. As regards the second function, we have no doubt that the recommendation of the Commission in respect of grants-in-aid would be given the utmost weight by the President and not ordinarily departed from by him.

70. The basis for the allocation of revenues referred to in item (a) should ordinarily be settled by the Commission at intervals of five years, but it should be open to the Commission to shorten the interval if it feels satisfied in special circumstances that such shortening is called for.

71. We would further recommend, in order to save time, that the Finance Commission may be set up in advance of the coming into effect of the Constitution, and its status regularised after the Constitution comes into effect.

Residuary Powers of Taxation

72. It appears that under the new Constitution, residuary powers will be vested in the Centre, so far as the Provinces are concerned, while the corresponding residuary powers in respect of the States will be vested in the States

themselves. The question has therefore been raised whether, as a consequence, as many specific taxes as possible should not be entered in the Provincial List of subjects. We cannot think of any important new tax that can be levied by the Provinces, which will not fall under one or the other of the existing categories included in the Provincial List. We think that the chance of any practical difficulty arising out of the proposed constitutional position is remote, and, in any case, it seems to us that if a tax is levied by the Centre under its residuary powers, there will be nothing to prevent the proceeds of the whole or a part of this tax being distributed for the benefit of the Provinces only. As a matter of abundant caution, however, it may be laid down in the Constitution that if any tax is levied by the Centre in future under it residuary powers, and to the extent that the States do not agree to accede to the Centre in respect of the corresponding subject, the whole or a part of the proceeds of the tax shall be distributed between the Provinces and the acceeding States only.

This disposes of item IX of our Terms of Reference

Exemption of Provincial Governments from Taxation

73. Section 155 of the Government of India Act provides that profits from trading by a Provincial Government would be taxable only if the trade was carried on outside the Province. The exemption from Central taxation of trade by Provincial Governments carried on within the provincial limits did not matter much in the past; for the Governments had few trading operations With the present tendency towards nationalisation (e g., many provinces have already taken up quite seriously the nationalisation of road transport) the Centre should have some power to levy either income-tax or a contribution in lieu of income-tax in respect of these trading activities. Disputes as to such contributions should, we consider, be examined and adjudicated upon by the Finance Commission to which we have already referred We feel that if nationalisation of industries or trades takes place rapidly, the whole question would have to be reviewed *de novo*, for the entire structure of the tax system of the country would be completely changed.

74. In the meantime we make the following recommendations —

(a) The existing practice should continue in respect of trading operations of the Central Government, i e., no income-tax should be levied on the profits It should be open to the Centre, however, to levy a contribution, as in the case of Railways, for its sole benefit from such operations. If the trading is carried on by a separate juristic person, tax will be levied even if the Government is the dominant shareholder

(b) Tax should be levied on the trading operations of Units (as also of local bodies), whether carried on within or without their jurisdiction; and the tax or the contribution in lieu thereof should be treated as ordinary income-tax revenue for the purpose of the divisible pool We presume that if there are no profits, there will be no contribution; but if this presumption is wrong, we suggest that the contribution should be treated as part of the divisible pool of income-tax.

c) We recommend that quasi-trading operations incidental to the ordinary functions of Government such as the sale of timber by the forest department or of jail products by the jail department should not be treated as trading operations for this purpose

Emergency Provisions

75. The needs of the Centre in times of emergency, such as war or large scale internal disorder, cannot be provided for through the detailed allocation of heads of revenue or of shares therein. It is obviously not possible to legislate how emergencies should be met. We would suggest that there should be a special provision in the Constitution authorising the President in an emergency to suspend or vary the financial provisions in such manner as he may think best in the circumstances. For example, if there is a war and an Excess Profits Tax is levied, it might be necessary for the Centre to retain the whole of this tax for itself.

Procedure in Financial Matters

76. Item X of our terms of reference is as follows:—

Is it necessary to make any modifications in the existing provisions as regards procedure in financial matters contained in Sections 33 to 37 and 78 to 83 of the Government of India Act, 1935?''

77. The present financial procedure in the federal sphere is laid down in sections 33-37 of the Government of India Act, 1935. The corresponding clauses in the Draft Constitution as prepared by the Secretariat of the Constituent Assembly are 74, 75 and 77-81. We have two recommendations to make:—

(1) When a money bill is sent from the Lower House to the Upper, a certificate of the Speaker of the Lower House saying that it is a money bill should be attached to, or endorsed on, the bill and a provision to that effect should be made in the Constitution on the lines of the correponding provision in the Parliament Act, 1911. This will prevent controversies about the matter outside the Lower House.

(2) After clause 80, a provision may be made making it necessary for Government to approach the Legislature for regularising any excess expenditure that might be discovered in audit after the close of the year. This is, in fact, done even now, but there is no statutory obligation to do so.

Subject to these two recommendations, we approve of the provisions in the Draft Constitution.

78. Financial procedure in the Provincial field is governed by sections 78-82 of the Government of India Act, 1935. The corresponding provisions in the Draft Constitution occur in clauses 149-153. We recommend:—

(1) that in a Province with a bicameral Legislature, if any, the powers of the Upper House over money bills should be exactly the same as at the federal level;

(2) that the new provision, in respect of a vote on excess grants, recommended by us at the federal level should be repeated at the provincial level also.

79. It is usual in written democratic constitutions to provide that no money can be drawn from the treasury except on the authority of the Legislature granted by an act of appropriation. In this country, the practice has been to authorise expenditure by resolutions of Government after the demands have been voted, and not by law. As the existing practice has been working well in this country, appropriation by law does not appear to be necessary.

Auditor-General

80. Though the question has not been specifically referred to us, we consider that the status and powers of the Auditor-General are so closely connected with financial procedure that we have gone into this matter also. The provisions in respect of the Auditor-General of the Federation are contained in clauses 106-109 of the Draft Constitution, and those in regard to the Auditor-General of the Provinces, in clauses 174-175. In substance, all these clauses repeat the existing provisions in the Government of India Act. We consider the provisions to be adequate for the purpose of securing the independence of the Auditor-General. We notice that the Auditor-General of India is to perform the functions of the Auditor-General in respect of the Provincial Governments also for an initial period of three years, and thereafter, until a particular Provincial Government chooses to appoint its own Auditor-General. We favour the continuance of a single Auditor-General for the Government of India as well as for the Provincial Governments, and it is possible that the Provincial Governments will also prefer that course, and will choose not to use their power of appointing separate Auditor-General of their own. The Draft Constitution, however, gives them the option to appoint Auditors-General if they think fit so to do. We are not sure whether it is possible altogether to do away with this option, much as we should like to do so; but if the option remains, we recommend that the provisions of sub-clause 3 of clause 174 should be amended so as to make the Auditor-General of a Province eligible for appointment as Auditor-General of another Province also.

Borrowing Powers

81. This question is covered by Item I of our Terms of Reference

The present position is that the Provinces have the freedom to borrow in the open market in India except when they are indebted to the Centre. The most outstanding advantage of the freedom of borrowing is the sense of financial responsibility it creates, for, there is no more accurate, sensitive and dependable meter of the credit of a borrowing Government than the reaction of the securities market. We do not therefore wish to withdraw this freedom. Nevertheless, it is necessary to have some machinery which would ensure that borrowing Governments do not, by their competition, upset the capital market. This machinery is now provided through the Reserve Bank which advises all the Governments, but in view of the ambitious programmes of development both by the Centre and by the Units, it may become necessary to set up some kind of expert machinery, both competent and definitely empowered, to fix the order of priority of the borrowings of the different Governments. In some countries, this co-ordination is effected either by a Ministerial Conference or by a Loans Council Such machinery should not affect the responsibility of a Government for its borrowing policy, and should help only in the timing of the loan and avoidance of unnecessary competition. The co-ordination by the Reserve Bank has worked well in practice; and so long as it works well we do not recommend any change. We assume that there will be no distinction between federating States and the Provinces in this respect.

82. We are of the opinion that it should not be open to a Provincial Government or to a Government of a State to go in for a foreign loan except with the consent of the Federal Government and except under such conditions, if any, as the Federal Government may think fit to impose at the time of granting the consent. We notice, however, that there is an entry, viz., "18. Foreign Loans" in the Federal Legislative List in the Draft Constitution.

we are not sure whether, the insertion of this entry in the Federal Legislative List is enough to prevent the Government of a Unit from going in for a foreign loan. We, therefore, recommend that the point be examined, and if the provision is not found to be adequate, a specific provision should be made in clause 210 of the Draft Constitution making it necessary for the Government of a Unit to obtain the consent of the Federal Government before going in for a foreign loan.

Problem of Indian States

83. The points at issue are contained in items III, IV, V, VI and XI of our terms of reference.

This part of our work is the most difficult party thereof, and the difficulty arises as much from the lack of statistical data as from the complications of the problem itself; for, not only do conditions differ widely between the Provinces as a whole and the States as a whole, but from State to State, so that it is difficult to apply a common yard-stick.

84. The Union Powers Committee of the Constituent Assembly in Para. 2 (d) of their report, dated 17th April, 1947, has expressed its view on this subject in the following terms:—"We realise that, in the matter of industrial development, the States are in varying degrees of advancement and conditions in British India and the States are in many respects dissimilar. Some of the above taxes are now regulated by agreements between the Government of India and the States. We, therefore, think that it may not be possible to impose a uniform standard of taxation throughout the Union all at once. We recommend that uniformity of taxation throughout the Units may, for an agreed period of years after the establishment of the Union not exceeding 15, be kept in abeyance and the incidences, levy, realisation and apportionment of the above taxes in the State Units shall be subjected to agreements between them and the Union Government. Provision should accordingly be made in the Constitution for implementing the above recommendation." We entirely agree with these observations.

85. We assume that the ultimate object of the Federation must be to secure for the federating States the same, or nearly the same standards of economic development, fiscal arrangements and administrative efficiency as in the Provinces. It is only against this background that the States can have the same identity of interest with the Union as the Provinces have.

86. The first difficulty met with in our investigation is that many of the smaller States have neither a budget nor effective audit, so that adequate and reliable information about their financial position, on a basis permitting comparison with Provinces, is not available. We recommend accordingly that it should be made obligatory within as short a period as possible for each State to arrange for the preparation and authorisation of a periodical budget and the maintenance of proper accounts and audit and to send copies of its budget, accounts and audit reports to the Union Government.

87. In the absence of sufficient data, we are not in a position to make recommendations other than of a general nature. We are clear in our mind that the States should gradually develop all the taxes in the Provincial Legislative List so that they may correspondingly give up reliance on taxes in the Federal Legislative List. This process however would necessarily take some time; and in the meanwhile it will be necessary to have transitional arrangements.

88. We will now take up Land Customs. We do not recommend the immediate abolition of Land Customs, for we find that such a course would lead to a serious dislocation in the finances of many States. Moreover, where there is no large re-export trade, these land customs, though a possible source

or annoyance, are really of the nature of octroi duty levied at a few points of entry. On a long view, however, in the interests of the States themselves, these duties might be replaced by other taxes, such as sales and turn-over taxes. We recommend accordingly that Land Customs now levied by the States should be abolished during the next 10 years. As a first step it may be arranged that—

(1) a State shall not in future levy land customs on a commodity on which there is no such duty now;

(2) a State shall not after a fixed date, increase the rate on any commodity; and

(3) a State levying land customs should grant refunds on re-exports.

Gradual abolition over a period of 10 years should not cause any serious dislocation to the finances of these States, nor can there be any question of paying any compensation to these States, for the simple reason that the Union Government will not gain any corresponding revenue

89. Maritime customs should be uniform all through the Union, and the Federal Government should take over the administration of such customs in all the maritime States. If this arrangement results in the loss of any State of the revenue now enjoyed by it, it is only fair that the State should be compensated for the loss. Pending determination of the appropriate compensation in each case by a States Commission, the appointment of which we recommend in a later paragraph, each State may be given an annual grant equal to the average revenue from this source during the last three years. The right of Kashmir to a rebate on sea customs may be similarly abolished on payment of a similar grant.

90. The Federal Government may levy Central Excises in all the States, but those States which now enjoy the benefit of a part or the whole of these revenues raised in their areas should, in lieu of such benefit, receive grants on the basis of the average revenue enjoyed by them from these sources during the last three years. In our opinion, neither this arrangement nor the one referred to in the foregoing paragraph should present any difficulty from the purely financial point of view either to the Union or to the States.

91. The Indian Income-Tax Act, with such modification as may be considered necessary by the President, may be applied to all the Federating States. The net proceeds of the tax attributed to the States may be credited to a States Income-Tax Pool and such portion not being less than 75 per cent. of the net proceeds attributable to each State, as determined by the President, may be paid back to the States.

We are aware that many problems will arise in the course of allocating these proceeds between the different states, but they are not insoluble, and can be solved on lines similar to those followed in allocating similar revenues between the Provinces.

92. The need for a uniform system of income-tax both in the Provinces and in the States has become urgent not only because of the facilities afforded for evasion and avoidance of the Central Income-tax by the existence of States with lower rates of taxation or no tax at all, but also because it is alleged that industries are being diverted artificially by the incentive of lower taxation to areas not inherently suited for the industries.

93. Though we do not favour any abrupt change in the *status quo*, we do not attach much weight to the argument that the States are, as a whole, industrially backward and that they cannot, therefore, stand the same high rates of taxation, particularly income-tax, as the Provinces can. If the productive capacity of a State and consequently its level of income, is low, it follows

that the State will not have to contribute much by way of tax if it falls in line with the Provinces. If, on the other hand, the point is that industries should be artificially stimulated in the States somehow by the incentive of lower taxes, it is obvious that if the State is not suited for industrial development, the cost of bolstering up its industries must ultimately fall upon the Provinces and other States.

94. As already stated, we are not in a position to make detailed recommendations regarding the States. We recommend for this purpose the establishment of a States Commission with five members who should possess wide knowledge of the financial administration of Provincial, Federal or State Governments. Preferably, one of these members might be a member of the Finance Commission (for Provinces) referred to earlier in this report. The Commission should advise the President, as also the States, about their financial systems and suggest methods by means of which the States could develop their resources and fall into line with the Provinces as quickly as possible. One of the first tasks of the Commission will be to examine in detail the privileges and immunities enjoyed by each State, and also the connected liabilities, if any, and recommend a suitable basis of compensation for the extinction of such rights and liabilities. We consider in particular that the States Commission should deal with the problems before it with understanding and sympathy and suggest solutions which would not only be fair both to the States and to the Provinces, but enable the States to come up to the Provincial standards in as short a time as possible.

95. The States which come into the above arrangements would pay their contribution for Defence and other Central services through the share of the net proceeds of Central taxes retained by the Centre, and nothing more should be expected from those States On the other hand, the States which accede but do not come into the above arrangements, should pay a contribution to the Centre, the amount of which should be determined by the States Commission having regard to all the relevant factors.

96 The constitutional arrangements in this respect, particularly during the interregnum of 15 years, should, in our opinion, be kept very flexible. The President should be enabled by order to adopt any financial arrangement he may find expedient with each State until such arrangement is altered by an Act of the Federal Legislature after necessary consultation with the States.

97 While the outlines which we have indicated above are capable of being applied to most of the major or even middle-sided States, it is, in our opinion, necessary to group together a number of smaller States in sizable administrative units before they can be brought into any reasonable financial pattern.

98. We are sorry that we have not been able to contribute anything more precise than we have done to this part of the terms of reference to us.

99. We enclose two Appendices (IV and V) one of which sets out in detail, as far as we have been able to collect, the rights and immunities enjoyed by various States, and the other setting out the total budgets of certain States and the part played by Land Customs in those budgets

Summary of Recommendations

100. (1) No major change to be made in the list of taxes in Federal Legislative List as recommended by the Union Powers Committee. (Para. 80)

(2) The limit of Rs. 50 to be raised to Rs. 250 for taxes on professions etc. levied by Local Bodies. (Para. 80)

(3) An entry to be made in the Federal Legislative List of a new item "Stock Exchanges and Futures Markets" etc. (Para. 80)

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(4) A few minor changes of a drafting nature to be made in the list of taxes in the Provincial Legislative List; and no new items for insertion in the Provincial Legislative List. (Paras. 31-33)

(5) The Centre to retain the whole of the net proceeds of the following taxes, viz. (a) Duties of Customs including Export Duties, (b) tax on capital value of assets, etc., (c) taxes on Railway fares and freights; and (d) Central Excises other than on tobacco. (Para. 34)

(6) The grant of fixed assignments for a period of years to the jute-growing provinces to make up for their loss of revenue. (Paras. 35-36)

(7) The net proceeds of the following taxes to be shared with the Provincial Governments, viz. (1) Income-tax, including Corporation Tax, (2) Central Excise on Tobacco; (3) Estate and Succession Duties. (Paras. 38-42)

(8) The suggestion that the Centre should be allotted only the excises on specified commodities, not accepted. (Para. 41)

(9) Federal Stamp Duties and Terminal taxes on goods, etc to be administered centrally, but wholly for the benefit of the provinces. (Paras. 43 and 44)

(10) Larger fixed subventions than now, necessary for Assam and Orissa, and subventions for limited periods for East Punjab and West Bengal, but no precise figures recommended for lack of data. (Paras. 45 and 46)

(11) Grants-in-aid on the Australian model not favoured (Para 48)

(12) Merging the tax on agricultural income in the Central Income-tax and similarly the Estate and Succession Duties on agricultural property in the similar duties on property in general to be examined in consultation with Provincial Governments and transfers made from the Provincial List of subjects, if necessary. (Para. 49)

(13) Not less than 60 per cent of the net proceeds of Income-tax, including Corporation Tax and the tax on Federal emoluments, to be divided between Provinces in the following manner:—

20 per cent. on the basis of population, 35 per cent. on the basis of collection and 5 per cent as an adjusting factor to mitigate hardship. (Paras. 55 and 56)

(14) Not less than 50 per cent. of the net proceeds of the excise on tobacco to be divided between Provinces on the basis of estimated consumption. (Para 57)

(15) Not less than 60 per cent of the net proceeds from Succession and Estate Duties to be divided between the Provinces on the following basis:—duties in respect of real property on the basis of allocation of the property, and of the balance, three-fourths on the basis of the residence of the deceased and one-fourth on the basis of population. (Para. 58)

(16) Net effect of the recommendations, to transfer annually a sum of the order of Rs. 30 crores from the Centre to the Provinces. (Para. 59)

(17) A Finance Commission with a High Court Judge or ex-High Court Judge as Chairman and four other members to be entrusted with the following functions:—viz (a) allocation between the Provinces of their shares of centrally administered taxes assigned to them; (b) to consider applications for grants-in-aid for Provinces and report thereon; (c) to consider and report on other matters referred to it by the President. (Paras. 65-67)

(18) The Commission to review the position every five years, or, in special circumstances, earlier. (Para. 70)

(19) A tax levied by the Centre under its residuary powers, not to enure to the benefit of a non-acceding State unless it agrees to accede to the Centre in respect of that subject. (Para. 72)

(20) Trading operations of Units, as also of Local Bodies, whether carried on within or without their jurisdiction, to be liable to Central Income-tax or a contribution in lieu, but quasi-trading operations incidental to the normal functions of Government not to be taxed. (Para. 74)

(21) The President to be empowered in an emergency to suspend or vary the normal financial provisions in the Constitution. (Para. 75)

(22) A few minor changes suggested in regard to the procedure in financial matters. (Para. 77)

(23) No change to be made in respect of borrowing powers of Units. (Paras. 81-82)

(24) Early arrangement to be made for the preparation of regular budgets and the maintenance of appropriate accounts and audit by all acceding States. (Para. 86).

(25) States gradually to develop all the taxes in the Provincial Legislative List and correspondingly give up taxes in the Federal List. (Para. 87)

(26) Maritime customs and excises in States to be taken over by the Centre, the States being compensated therefor if necessary. (Paras. 89 and 90)

(27) The Indian Income-tax Act to be applied to all the federating States, and 75 per cent. of the net proceeds attributable to the States to be divided between them. (Para. 91)

(28) A States Commission to be set up with five members with wide knowledge of the financial administration of Provincial, Federal or State Governments. (Para. 94)

(29) The States Commission to examine the privileges and immunities etc. of States and to suggest suitable compensation for the extinction of these rights and liabilities. (Para. 94)

(30) States which do not come into the arrangements to pay a contribution to the Centre to be determined by the States Commission. (Para. 95)

(31) The *interim* Constitutional arrangements with the States to be flexible and small States to be grouped together. (Paras. 96 and 97)

Conclusion

101. Some of our recommendations would need to be embodied in the Constitution while others would be given effect to by the order of the President. We have attempted a draft of the necessary provisions in the Constitution to give effect to the former; and these are set out in Appendix VI.

102. Mr. Rangachari has signed this report in his personal capacity, and the views expressed in it should not be treated as committing in any manner the Ministry of Finance of which he is an officer.

NALINI RANJAN SARKER,
V. S. SUNDARAM,
M. V. RANGACHARI.

New Delhi,
December 5, 1947.

APPENDIX I

CONSTITUTIONAL POSITION OF THE CENTRE AND THE PROVINCES IN RESPECT OF REVENUE UNDER THE GOVERNMENT OF INDIA ACT, 1935

(a) Revenues of the Federation

(1) From Taxes

- **A. Levied and collected by the Federation but belonging wholly to the Provinces or Units.**
  1. Duties on Succession to property other than agricultural land.*
  2. Stamp Duties on Bills of Exchange, Cheques, Pro-notes, Bills of Lading, Letters of Credit, Policies of Insurance, Proxies and Receipts. †
  3. Terminal Taxes on goods or passengers carried by Railway or air. ‡
  4. Taxes on Railway fares and freights.*

  (Subject to the right of the Federation to raise Federal Revenue by a surcharge on all the items in this list.)

- **B. Levied and collected by the Federal Government of which a portion is or may be assigned to the Provinces**
  - a. Assigned by the Act.
    1. Income-tax other than Corporation Tax. (Subject to Federal Surcharge)¶
    2. Jute Export Duty.¶
  - b. May be assigned by Federal Law.
    1. Duty on Salt.§
    2. Other duties of Excise on Tobacco and on other Goods manufactured or produced in India except
       (a) alcoholic liquor for human consumption
       (b) Opium, hemp, a d other narcotics and non-narcotic drugs.
       (c) medicinal and toilet preparations ‖
    3. Duties of Export. ‖

- **C. Levied and collected by Federation and, belonging wholly to the Federation.**
  1. Taxes in Lists A & B in areas administered by the Federal Government.
  2. Customs.
  3. Corporation Tax.
  4. Surcharges mentioned in Lists A & B
  5. Taxes on capital values of assets of individuals and companies.
  6. Miscellaneous receipts fro n fees in respect of matters in Federal List (including fees taken in the Federal Court.)

(2) From Commercial Operations.

1. Posts & Telegraph.
2. Federal Railways.
3. Banking.
4. Other Commercial Operations.

(3) Sovereign Functions

1. Coinage and Currency.
2. Escheat and lapse in areas administered by Federal Government.

(4) Contributions from States—Assigned by His Majesty.

- Tributes and other payments.

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* Not yet levied.

† These duties continue to be both levied and collected by the Pro nces.

‡ Levied so far only for the benefit of local bodies.

¶ See notes under the other Table.

§ Duty now abolished.

‖ No share assigned to Provinces.

(b) Revenues of the Province

- A By Taxes
  - A. Directly raised by the Province.
    1. Land Revenue.
    2. Duties of excise on alcoholic liquors, etc., excluded from Federal revenues.
    3. Taxes on Agricultural income.
    4. Taxes on lands and Buildings* Hearths and Windows
    5. Succession to agricultural land.
    6. Taxes on Mineral rights.
    7. Capitation taxes.
    8. Taxes on Professions, Arts, Trades and Callings.*
    9. Animals and Boats.*
    10. Sale of Goods and Advertisements.
    11. Octroi.
    12. Taxes on luxuries, entertainments, etc.*
    13. Stamps—other than Stamps in Federal List.
    14. Taxes on Passengers and Goods in inland waterways.
    15. Tolls†.
    16. Miscellaneous Receipts from fees including fees taken in Courts (other than the Federal Court.)
  - B. Levied and collected by the Federation and wholly allocated to the Provinces
    - Items in List A of the other Table.
  - C Levied and Collected by the Federation but which is or may be allocated in part to the Provinces.
    - (a) By the Government of India Act
      - Income-Tax.‡
      - Export duty on Jute.¶
    - (b) By Federal Legislation.§
      - Salt.†
      - Federal Excise Duty.
      - Export Duties‖.
- B. Commercial Operations.
- C. Sovereign Rights.
  - Escheat and Lapse.
- D. Grants-in-aid and subventions from the Center

* These taxes are now raised by Municipal and other Local authorities for their needs

† Now abolished—but before abolition was a source of Municipal Taxation.

‡ By order in Council 50% of the net proceeds of tax on income other than Corporation Tax exclusive of proceeds attributable to Chief Commissioners' Provinces and taxes in respect of Federal emoluments are distributable in accordance with a prescribed ratio

¶ 62½ assigned to Provinces by Order in Council distributed among jute producing Provinces in proportion to the respective amounts of Jute grown in them.

§ Duty abolished.

‖ No share allotted to Provinces.

APPENDIX II

FINANCIAL POSITION OF THE PROVINCES AND THE CENTRE FROM 1937-38 TO 1946-47

(a) Provinces

(In lakhs of Rupees)

Province	Provincial Revenue	Devolution Grants from the Centre including Dev. Grants	Total Revenue	Total Revenue Expenditure	Cumulative Deficit (—) Surplus (+)	Balances in Reserve Funds on 31st, March 1947	Closing balance on 31st March 1947
Madras	2,63,27	24,12	2,87,39	2,84,22	+ 3,17	29,18	56
Bombay	1,92,52	26,51	2,19,03	2,06,69	+12,34	17,07	42
Bengal	1,65,35*	69,92	2,35,27	2,51,13*	—15,86	25	2,48
United Provinces	1,79,33	26,77	2,06,10	2,04,99	+ 1,11	17,31	6,43
Panjab	1,84,12	11,51	1,95,63	1,60,46	+35,17	6,79	57
Bihar	75,06	15,10	90,16	81,81	+ 8,35	7,78	1,07
C. P. & Berar	63,61	7,69	71,30	70,66	+ 64	8,14	2,41
Assam	35,54	7,89	43,43	42,89	+ 54	1,02	1,54
N. W. F. P.	11,94	11,55	23,49	22,95	+ 54	15	63
Orissa	17,71	7,93	25,64	25,11	+ 53	10	60
Sind	55,19	10,27†	65,46	60,04	+ 5,42	8,14	8

*Subsidy of 3,00 in 1943-44 taken by Bengal as reduction of Expenditure on Famine. Hence Revenue and Expenditure both have been increased by 3,00.

†The subvention was capitalised on 1st April 1944 and the value set off against the Lloyd Barrage Debt.

Revised Estimates have generally been taken for 1946-47.

(b) Central Government (1937-38 to 1946-47)

(In lakhs of Rupees)

Year	Revenue	Expenditure			Deficit(—) Surplus (+)
		Civil	Defence	Total	
1937-38	86,61	39,39	47,22	86,61	..
1938-39	84,52	38,97	46,18	85,15	—63
1939-40	94,57	45,03	49,54	94,57	..
1940-41	1,07,65	40,57	73,61	1,14,18	—6,53
1941-42	1,34.57	43,33	1,03,93	1,47,26	—12,69
1942-43	1,77,12	74,28	2,14,62	2,88,90	—1,11,78
1943-44	2,49,95	81,44	3,58,40	4,39,84	—1,89,89
1944-45	3,35,71	1,00,77	3,95,49	4,96,26	—1,60,55
1945-46	3,61,18	1,24,38	3,60,23	4,84,61	—1,23,43
1946-47 (Revised Estimate)	3,36,19	1,43,36	2,38,11	3,81,47	—45,28
TOTAL	19,68,07	7,21,52	18,87,33	26,18,85	—6,50,78

The amounts included in the above on account of revenue assigned to the Provinces and Grants-in-Aid and Subventions to them are given below :—

(In lakhs of Rupees)

Year	Share of Jute Export Duty	Share of Income-tax	Grants-in-aid and Subventions
1937-38	2,65	1,25	3,14
1938-39	2,51	1,50	3,05
1939-40	2,56	2,79	3,04
1940-41	1,85	4,16	3,04
1941-42	1,95	7,39	3,03
1942-43	1,40	10,90	2,76
1943-44	1,38	19,50	5,75(a)
1944-45	1,49	26,56	8,70(b)
1945-46	1,57	28,75	9,70(c)
1946-47 (Revised Estimate)	2,80	29,87	1,70
TOTAL	20,16	1,32,67	43,91(d)

(a) Includes 3,00 Special Grant to Bengal.
(b) Includes 7,00 Special Grant to Bengal.
(c) Includes 8,00 Special Grant to Bengal.
(d) Includes 7 roundly in all for Coorg.

APPENDIX III

SUMMARY OF PROVINCIAL SUGGESTIONS
Part I—Taxes

Tax 1	Assignment existing or contemplated 2	Provinces proposing 3	Assignment proposed for provinces 4
1. Income tax (other than on agricultural income). [Sec. 138 of the Government of India Act, 1935 and item 54 in Federal Legislative List.]	A maximum of 50% of the net proceeds to be distributed among provinces.	Madras .	A minimum of 50% of net proceeds.
		Bombay .	75% of income tax and corporation tax receipts for provinces or 75% of the corporation, income and super taxes paid by residents in a province to be earmarked for that province. From the divisible pool from corporation and income tax 33⅓% should be allotted to Bombay which is the largest single contributor to the revenue.
		U. P. . .	50% for provinces on population basis.
		C. P. . .	75%. Tax on Agricultural income also should be collected by centre.
		West Bengal	60% to be distributed in proportion to the collection of these taxes in provinces.
		Bihar . .	Even on the basis of population Bihar should have received 17 crores as against 13 allotted. In future none of the poorer provinces should get an amount lower than that payable on the basis of population. The distribution should be governed not by residence of the assessees but by the place where the income is earned. The basic factors must be population and the place where the income is earned. If any modifications are to be made they must be done with the object of assisting the financially poorer provinces among which Bihar is at the very bottom.
		Orissa	Distribution of 50% may continue as at present; but the percentages should be revised taking into consideration the factor also of the state of development in addition to those of population and residence used by Sir Otto. Due weightage to be given to undeveloped provinces. Should the provincial share exceed 12 crores, 75% of the excess may be left to the discretion of the Central Government.

1	2	3	4
		East Punjab	After the partition the East Punjab Province faces a deficit of about 3 crores ; its share of income tax proceeds should be very appreciably increased to meet the deficit fully
		Assam .	75%. There should be a drastic revision of the shares of provinces in income tax receipts having regard to the facts that Sind and N W F P go out, that the amounts now available in the divisible pool have enormously exceeded the original estimate and some provinces are now getting, as a result, income tax amounts exceeding the entire revenues of some others.
2. Corporation Tax. (Item 46 in Federal Leg. List)	Wholly Federal .	Madras .	At least 50% of the net proceeds to go to provinces.
		Bombay	75% for provinces
		U.P. .	50% for provinces on population basis
		C.P	C P suggests the inclusion of Corporation tax and taxes on Capital and Capital Assets in taxes on income for distribution
3. Central Excise duties (on tobacco and other goods except alcoholic liquors (item 46)	There is provision for sharing in full or in part [Sec. 140 (1)] but not so far shared.	Madras .	Should be entirely provincialized
		Bombay .	Should be provincialized or not less than 50% of the net proceeds in each producing unit to be allotted to that unit.
		U.P .	Should be entirely provincialized and distributed on population basis.
		C P	Should be provincialized or 75% should be allotted to provinces. The duty should cover some more articles such as rubber goods, papers, etc.
		West Bengal	25% of the federal excise should be allocated to provinces.
		Bihar .	A portion of the duty should be distributed on the basis of the yields in different Provinces
		Orissa . .	A portion may be distributed to provinces gradually particularly as the provinces are now faced with the loss of their excise revenue.
		Assam .	At least 75 per cent. of the excise duty collected on her oil should be allotted to Assam. At least 50 per cent. of the other excise duties (Sugar, Steel, Matches, Tobacco and Beetle Nuts) to be given to the producing units on a

1	2	3	4
			formula combining factors of province of production, size of population and level of revenue expenditure.
4. Export Duties on Jute and Jute products.	62 ½ per cent. of net proceeds) [Section 140 (2)].	West Bengal.	75 per cent. should accrue to the provinces growing and manufacturing jute.
		Bihar . .	The entire net proceeds of the jute producing provinces should be distributed proportionately among the concerned provinces
5. Export Duties .	....	Madras .	At least 50 per cent. of net proceeds of all export duties should be distributed to provinces according to principles formulated by Federal Legislature. Analogy of jute duty arrangement cited
		Bombay .	50 per cent. of net proceeds.
		U. P. . .	All export duties should be entirely provincialized and distributed on population basis
		C. P. . .	Export duty on minerals (Coal and Manganese, etc.), should be allotted to C. P. (Jute analogy).
		West Bengal.	25 per cent. of net proceeds of export duties other than jute'
		Orissa . .	A portion may be distributed to provinces gradually particularly as the provinces are now faced with the loss of their excise revenue
		Assam .	At least 75 per cent. of the sale proceeds of export duty realised on her tea.
6. Succession duties, Federal Stamp duties, Terminal taxes (Railway & Air), Taxes on Railway Fares & Freights.	Provided for full distribution to provinces. (Sec. 137).	Madras .	It should be provided that the net proceeds shall not form part of the Revenues of the Federation but shall be distributed to the provinces according to principles formulated by the Federation
		U. P. . .	The provisions should be fully utilized to augment the resources of provinces.
		C. P. . .	Succession duties in respect also of agricultural land should be transferred from the provincial to the Federal list. The duty should be on *ad valorem* basis.
		West Bengal.	The provincial governments should be empowered to levy them if the Central Government do not levy them.

1	2	3	4
		Assam	50 per cent. of income from increase in railway fares and freights above the levels determined by the Railway Budget of February 1947 to go to provinces on population ratios weighted by a given factor in favour of provinces with smaller revenues and expenditure.
7. State Lotteries	Federal (item 48 Federal List).	C. P.	Should be transferred to Provincial list.
8. Taxes on trades, professions, callings and employment.	Provincial tax, Sec. 142-A, Item 46 in Provincial list.		The limit of Rs. 50 p. a. should be removed and gradation according to capacity should be provided for.
9. Taxes on sales and advertisements.	(Item 48 in Provincial list).		Sales tax should be levied in all provinces and acceding states.

Part II—Non-tax proposals

U. P. . .	(1) The inequity of the Niemeye Award should be rectified and the central allocation for U. P. should aim at a minimum of 6 or 7 crores p.a. going up to 12 or 13 crores in the space of 10 years. (2) The consolidated debt due from the U. P. to the Government of India should be wiped off. (3) The Government of India should share losses on the food grains scheme as originally promised by them.
C. P. . .	A system of central grants derived after taking into account such factors as natural resources, stage of industrial development, taxable capacity, etc., is essential. An expert financial enquiry should be undertaken.
West Bengal.	(1) Provision for federal aid to provinces for social and amelioration work. (2) There should be a finance commission on the lines of the Commonwealth Grants Commission in Australia.
Bihar . .	If any grants-in-aid or subventions are given in future the per capita revenue and expenditure in each province during the last ten years should be kept in mind. Those with low per capita revenue and expenditure should be given greater assistance than the richer.
Orissa . .	The broad lines of the present allocation may be maintained in the new Constitution; but the subvention of 40 lakhs fixed for the province should be increased; it should be

1	2	3	4
			stated as a percentage of the revenues of the central government and in any case there should be a minimum annual subvention of 150 lakhs.
			Enforcement of the policy of prohibition and judicial panchayats will make the provincial administration impossible unless the Central Government multiplies its grants and subventions very liberally.
			Abolition of the Zamindari system would seriously affect Land revenue and stamps. Make every one pay according to his capacity. Provide for a well regularised house tax on a provincial scale; a tax on passengers.
			Nationalization of industry will wash away the twin anchor sheets of Central finance—Income tax and Customs.
		East Punjab	(1) Particularly as the East Punjab is now to be the frontier of the Indian Dominion, there is a strong case for a recurring subvention of more than 1 crore for it (N. W. F. P. used to get 1 crore).
			(2) A non-recurring subvention for the capital of the province. (Orissa was given such a grant).
		Assam	There is an obvious case for an upward revision of the subventions granted to Orissa and Assam.
			Assam as a frontier as well as a backward province of India deserves special treatment.
			Its royalty of 5 per cent. on oil (as against 10 times that amount of central excise) is unfair. Large amounts of income accrue in Assam but are assessed in Calcutta which is headquarters of the concerned companies. Some provinces like Bombay and Benga have been allowed to get a large share of increase tax receipts because of their claim to be territorially responsible for the production of the incomes. Assam is entitled to similar consideration in regard to certain items of central revenues.

APPENDIX IV

RIGHTS AND IMMUNITIES ENJOYED BY THE STATES

(A) annual value of the immunities enjoyed by the States under sea Customs currency and coinage.

State	Year to which the figures relate	Rs. in lakhs	Remarks (see footnote)
(i) Sea Customs			
Kutch	1945-46	21·18	(1)
Bhavnagar	Do.	·19	(2)
Morvi	Do.	6·80	(3)
Junagadh (excluding Mangrol)	Do.	12·65	(3)
Nawanagar	Do.	15·27	(3)
Porbandar	Do.	3·63	(3)
Cambay	Do.	2 00	(4)
Baroda	1943-44	22·98	(5)
Janjira	1945-46	3·00	(6)
Cochin	1944-45	22·70	(7)
Travancore	Do.	17·99	(7)
Sawantwadi	Do.	0·12	(8)
Mangrol	Do.	2·33	(9)
Kashmir	1945-46	11·00	(10)
(ii) Currency and Coinage			
Hyderabad	1945-46	105·55	

(6th October 1945—5th October 1946).

FOOTNOTE

(1) In connection with Federation, the proposed method of calculating the immunity in the case of Kutch was as follows:—

To the trade figures supplied by the State the British Indian tariff rates should be applied and from this total should be deducted the difference between the duty calculated at British Indian tariff rates and that actually collected at State rates on goods not consumed in the State itself.

As the figures necessary to apply this formula are not available the figure given in the statement represents simply the amounts of customs duty retained by the State in 1945-46.

(2) The value of the immunity in the case of Bhavnagar is the total of customs collections made and retained by the State. The figures for 1945-46 is abnormal.

The figures for 1930-31 to 1935-36 were as follows:—

Year.	Rs.
1930-31	51,02,974
1931-32	75,91,016
1932-33	81,93,368
1933-34	99,32,628
1934-35	1,21,55,668
1935-36	61,62,300

(3) The value of the immunity in these cases is represented by the total customs collections less the amount payable to the Central Government under the Agreements.

(4) By the agreement of 1938 Cambay is allowed to retain whichever is greater of the following two amounts:—

(i) Rs. 2 lakhs; or

(ii) a proportion of the customs duties collected at the State ports on the basis of population with suitable adjustments to correct difference between the proportion of the urban population to the rural population in the state and the whole of India respectively.
Since the net customs revenue collected by the State during 1945-46 was only Rs. 6,993/- the State was entitled to receive from the Central Government the difference between that figure and Rs. 2 lakhs. The immunity in this case in therefore R 2 lakhs.

(5) Baroda is entitled to retain all the duty collected by it up to a maximum of 1 per cent of the average customs revenue of British India and until this maximum is reached, the immunity is represented by the State's collections. The latest figures available are given here.

(6) Annual payment under the 1940 Agreement, which represents the State's immunity.

(7) The immunity of Travancore and Cochin is represented by their share of the pool produced by the collection of duty at the British port of Cochin, at Cochin ports and Travancore backwaters. In addition it is necessary to include for Travancore the annual collections of customs duty at their ports other than the backwater ports; and in respect of commodities such as tobacco, on which Travancore levies duty at rates other than British Indian rates, the amount of duty at those rates is substituted for the actual collections.

(8) The immunity is represented by the compensation payment of Rs. 13,433 less Rs. 1,700 allotted for abolition of land-customs under the Agreement of 1938.

(9) Actual amount collected and retained by the State.

(10) Drawback from customs on goods imported by sea through British India.

(B) Note prepared by the Ministry of States on excise arrangements with States

Matches.—In respect of match excise there is a pooling arrangement with the States. The main principle is that the whole of the proceeds of the tax collected in any State are made over to the general pool and the whole proceeds of the pool divided between British India on the one hand and the various States that agree to come into the pool on the other on the basis of population, regardless of whether matches are manufactured or not, in the States. Import of matches from the States that have not joined this arrangement, is prohibited. The conditions that a State is required to accept for admission to the pool are—

(a) The State should levy duty on matches produced in their territories by means of British Indian bandemls and pay the proceeds into the common pool.

(b) The British Indian procedure for the levy and collection of duty should be followed.

Licence fees and fines are not included in the pool. Deduction on account of collection charges at a uniform rate is allowed. The present rate is 3 per cent of the net collections. The total net revenue is distributed among the various States and British India on the basis of population. While the amount contributed by States during 1944-45 to the pool was Rs. 44,38,970 the amount actually paid to the States was Rs. 1,00,66,875. The British Indian realisation was Rs. 5,46,26,781.

* * *

3. **Sugar**.—Arrangements were made in 1934 with the sugar producing States whereby they were required to levy the same rates of excise and under the same conditions as in force in British India in return for which sugar produced in Indian States was to be admitted free to British India. Soon after the outbreak of war, arrangements were made with the major sugar producing States, whereby in addition to compliance with the 1934 arrangements, these States undertook to hand over to the Central Government the excess of their earnings from sugar excise in any year above the highest revenue derived from the sugar excise in any of the three years preceding 1939-40. As regards States which had not till then developed a degree of production materially in excess of their own consumption and States which had not commenced production the Residents were asked to watch and report developments. All producing States were, however, requested to levy the same duty as in British India. In the case of such States where production now exceeds consumption, the arrangement is that the State retains duty on the basis of population at the rate of Rs. 3/20 per capita revenue.

The sugar producing States are—

A	B
Mysore	Baroda
Phaltan	Hyderabad
Kolhapur	Udaipur
Kapurthala	Gwalior
Rampur	Aundh
Jaora	Nabha
Bhopal	Kashmir
Sangli	
Miraj	

The States falling in category A above produce sugar in excess of their requirements and those falling in category B less than their requirements. Of the first mentioned States, negotiations were satisfactorily concluded with the first five. Bhopal which is surrounded on three sides and Jaora which is surrounded on all sides by Indian States, taking full advantage of their geographical position did not accept the settlement at first. Jaora, however, agreed to surrender its surplus revenue from 1942-43. Sangli and Miraj States only recently developed their sugar factories and have agreed to surrender the surplus revenue on the basis of the formula at 'A' above but have protested for revision of the arbitrary figure of actual consumption represented by 3/20ths. The matter is under consideration

The amount retainable by Indian States and the average duty collected are as follows:—

Name of State	Amount retainable	Average collection
	Rs.	(Rs. in lakhs)
Mysore	12,91,135	17
Kapurthala	2,52,000	8
Kolhapur	2,33,592	4
Rampur	11,43,532	16
Phaltan	5,21,262	8
Sangli	44,007	Not known
Miraj	6,944	Not known

Following is the contribution by the above States to the Central Exchequer in respect of the year 1945-46—

	Rs.
Mysore	...
Kapurthala	6,47,368
Kolhapur	2,26,820
Rampur	...
Phaltan	1,40,585
Sangli	1,07,869
Miraj	59,268

Information regarding the amount to be surrendered by Mysore and Rampur, is still awaited.

* * * * * *

7. **Tobacco.**—All States are expected to levy the British Indian rate of duty. (Some States where production is not of much consequence levy excise on the basis of acreage in view of the high cost of administration.) The States are entitled to retain the proceeds of the excise duty subject to the limit, on the basis of their population, worked out in accordance with the following formula—

$$A \quad \frac{R \times p}{P}$$

Where A is the limit retainable by a State;

R, the total net revenue in any year calculated from 1st April to 31st March, collected in British India and all the participating States (i.e., the gross revenue less the cost of collection, licence fees, penalties, fines etc.);

p, the population of the State concerned;

P, the population of British India and all the participating States.

Some States have not come into the scheme and the tobacco of such States on entry into British India is confiscated and released on payment of fine and penalty. Although section 5 of the Central Excises and Salt Act 1944 empowers us to impose customs duty equivalent to the excise duty, the provisions of this section have not been involved because it has been possible to realise an amount equivalent to the excise duty on State Tobacco under rule 82 of the Central Excise Rules by means of confiscation. Hyderabad has not accepted the formula and does not share the revenue with the Government of India although it has legislated on the lines of British India. No restrictions have been imposed on the entry of Hyderabad Tobacco into British India.

To facilitate movement of tobacco from and to the States, a special procedure for the movement in bond has been devised. Under this procedure the duty is realised at destination and credited to a Suspense account. The amounts realised on the State tobacco is at the end of the year credited to the State and is taken into account in the State's realisations for purposes of the formula. The revenue contributable by the States during the year 1943-44 and 1944-45 were Rs. 51,38,809 and Rs. 1,48,07,552 respectively.

8. **Vegetable Product.**—The formula is the same as in respect of tobacco. The only States concerned at present are Mysore and Cochin although the other States were asked to legislate and have legislated on the matter. Of the two States, namely, Cochin and Mysore, Cochin's contribution to the Central Revenues during the year 1943-44 and 1944-45 was Rs. 76,160 and Rs. 41,212 respectively. The Mysore State has nothing to pay under the formula.

9. **Tea, Coffee and Betel Nuts.**—The States concerned are:—

Tea:—Mysore, Travancore, Cochin; Tripura, Mandi;

Coffee:—Mysore, Travancore, Cochin;

Betal Nuts: Mysore, Travancore, Cochin, Tripura, Sawantwadi and Janjira.

The rates of duty imposed by Travancore are as follows: —

Betal Nut . .	As. 1/6	per lb.
Coffee . . .	,, -/6	,, ,,
Tea . . .	,, 1/9	,, ,,

The same formula as in respect of tobacco has been adopted in respect of these excises also, although the Board's intention was that 'P' in respect of these excises should denote the population of all India and not limited to participating States and British India as in the case of tobacco. Mysore and Travancore, the two important States, have been clamouring for a revision of the formula. In the case of Travancore the following revised formula has been offered:—

$$a = \frac{T}{P}$$

Where a denotes per capita consumption figure;

T, the total quantity of the article taxed in British India and in other participating units,

P, the total population of British India and other participating States.

On the basis of the per capita consumption figure worked olt, the amount retainable by the State will be worked on the basis of the following formula.

$$A = a \times d \times p$$

Where A = amount retainable by the State:

a = per capita consumption figure of British India and the participating units;

d = rate of excise duty levied by the State;

p = Population of Travancore.

The excess over 'A' plus cost of collection will have to be surrendered by the State. The State's acceptance of the formula has not yet been received.

In the case of Mysore, we have agreed in respect of coffee that the amount retainable by the State may be determined on the basis of the Coffee Controller's statistics of coffee consumption in the State. Mysore has accepted this formula and is pressing for a similar formula in respect of betel nuts. After a recent tour, the Board has stated that after the establishment of the Betal Nut Marketing Board, it may be possible to adopt the coffee formula in respect of betel nuts also.

(C) Statement showing the value of service postage stamps supplied annually free to States

S. No.	Name of State	Value
I		Rs.
1	Alwar	30,000
2	Baroda	1,25,000
3	Bharatpur	12,000
4	Bhopal	8,380
5	Bikaner	37,000
6	Bushahr	600
7	Cooch Behar	9,000
8	Datia	5,000
9	Dhar	3,000
10	Faridkot	1,000
11	Gwalior	480
12	Idar	550
13	Indore	35,000
14	Jhalawar	2,400
15	Jabbal	250
16	Kalsia	450
17	Kashmir	20,000
18	Kotah	15,000
19	Loharu	300
20	Malerkotla	900
21	Mandi	700
22	Marwar	39,000
23	Panna	900
24	Sikkim	1,500
25	Sirmoor	1,275
26	Suket	700

(D) Statement showing the values of immunities granted annually to Indian States in the shape of free conveyance of their official correspondence within the State limits

Name of the State	Value of the immunity	Remarks
	Rs.	
(1) Mysore	21,38,182	
(2) Hyderabad	5,440	Combined figure for the portions of the State in the Madras and Bombay Circles.
(3) Banganapalle	365	
(4) Pudukottai	37,960	
(5) Baroda	14,705	
(6) Ebor	68	
(7) Jawhar	3,627	
(8) Bhopal	149,177	
(9) Rewah	1,72,380	

(E) Statement showing the amounts of telephone revenue accruing in India on behalf of Indian States and *vice versa*

Amount of revenue accruing in India on behalf of States

	1944-45	1945-46	1946-47
	Rs.	Rs.	Rs.
1. Kashmir	1,912 3 0	2,731 3 0	1,646 13 0
2. Jammu Tawi	3,880 0 0	4,475 5 0	4,005 4 0

Amount of revenue accruing in States on behalf of India

	1944-45	1945-46	1946-47
	Rs.	Rs.	Rs.
1. Kashmir	1,702 5 0	2,375 1 0	1,187 7 0
2. Jammu Tawi	3,608 1 0	4,133 12 0	1,501 3 0

APPENDIX V

STATEMENT SHOWING REVENUE AND THE PERCENTAGE OF LAND CUSTOMS INCLUDED IN THE REVENUE OF CERTAIN STATES

(In lakhs of Rupees)

S.No.	Name of State	Total Revenue (Ordinary)	Land Customs	Percentage	Remarks
1	2	3	4	5	6
1	Hyderabad . .	943	124	13·2	
2	Travancore . .	611	89	14·6	
3	Kashmir . .	557	117	21·0	
4	Gwalior . .	303	41	13 5	
5	Jaipur . . .	197	23	11·6	
6	Baroda . . .	434	20*	4·6	*Includes Sea Customs, figures of which are not separately available.
7	Jodhpur . .	224	40	17·8	
8	Udaipur (Mewar) .	81	1	1 3	
9	Indore . . .	305	27	8·9	
10	Bikaner . .	252	29	11·5	
11	Alwar . . .	90	44	48 9	
12	Bhopal . . .	124	20	16·1	
13	Kotah . . .	48	6	12·5	
14	Tehri-Garhwal .	23	4†	17·4	†Includes Excise also.
15	Bharatpur . .	65	23	35·4	
16	Cutch . . .	89	1	1·1	
17	Patna . . .	30	6	20 0	
18	Sarguja . .	17	5	29·4	
19	Nawanagar . .	110	19‡	17·3	‡Inculdes Sea Customs, figures of which are not separately available.
20	Tonk . . .	34	11	32·3	
21	Bundi . . .	29	8	27·6	
22	Sirohi . . .	21	4	19·0	
23	Dungarpur . .	22	8	36·4	
24	Banswara . .	13	3	23·1	
25	Partabgarh . .	8	3	37·5	
26	Jhalawar . .	7	1	14·3	
27	Jaiselmer . .	6	3	50·0	
28	Shahpura . .	4	1	25·0	
29	Danta . . .	3	1	33·3	
30	Palanpur . .	28	5	17·9	
31	Idar . . .	45	17	37·8	
32	Balasinor . .	5	1	20·0	
33	Lunawada . .	10	2	20·0	
34	Sant . . .	12	2	16·7	
35	Chhota Udaipur .	24	2	8·3	
36	Radhanpur . .	23	4	17·4	
37	Baria . . .	18	1	5·6	
38	Dewas (Junior) .	23	4	17·4	
39	Panna . . .	10	1§	10·0	§Includes Tributes &c.
40	Ratlam . .	17	6	35·3	
41	Alirajpur . .	6	1‖	16·7	‖Includes Sayar.
42	Bijawar . .	7	1¶	14·3	¶Includes Biyai.
43	Chhatarpur . .	5	2	40·0	
44	Barwani . .	12	2	16·6	
45	Jaora . . .	22	3	13·6	
46	Rajgarh . .	12	1	8·3	
47	Sailana . . .	6	1	16·6	
48	Jhabua . . .	13	4	30·8	

APPENDIX VI

AMENDMENTS RECOMMENDED IN THE DRAFT CONSTITUTION

Provisions relating to procedure in financial matters

Clause 75.—To clause 75 *add* the following, namely:—

"(4) There shall be endorsed on every Money Bill when it is transmitted to the Council of States under Section 74, and when it is presented to the President for assent under section 76, the certificate of the Speaker of the House of the People signed by him that it is a Money Bill."

Clause 79:—In sub-clause (3) of clause 79, for the words "succeeding section" *substitute* the words "two succeeding sections"

New clause 80-A.—After clause 80, *insert* the following new clause, namely:—

"80-A ***Excess grants.***—If in any financial year expenditure from the revenues of the Federation has been incurred on any service for which the vote of the House of the People is necessary in excess of the amount granted for that service and for that year, a demand for the excess shall be presented to the House of the People and the provisions of sections 78 and 79 shall have effect in relation to such demand as they have effect in relation to a demand for a grant."

Clause 145.—For sub-clause (1) of clause 145, *substitute* the following, namely:—

"(1) Subject to the special provisions of this Part of this Constitution with respect to Money Bills, a Bill may originate in either House of the Legislature of a Province which has a Legislative Council.

(1a) Subject to the provisions of sections 146 and 146-A, a Bill shall not be deemed to have been passed by the Houses of the Legislature of a Province having a Legislative Council unless it has been agreed to by both Houses either without amendments or with such amendments only as are agreed to by both Houses"

Clause 146.—For clause 146, *substitute* the following, namely:—

"**146.** ***Passing of Bills other than Money Bills in Provinces having Legislative Councils.***—(1) If a Bill which has been passed by the Legislative Assembly of a Province having a Legislative Council and transmitted to the Legislative Council is not, before the expiration of twelve months from its reception by the Council, presented to the Governor for his assent, the Governor may summon the Houses to meet in a joint sitting for the purpose of deliberating and voting on the Bill:

Provided that nothing in this section shall apply to a Money Bill.

(2) If at a joint sitting of the two Houses summoned in accordance with the provisions of this section the Bill, with such amendments, if any, as are agreed to in joint sitting is passed by a majority of the total number of members of both Houses present and voting, it shall be deemed for the purposes of this Constitution to have been passed by both Houses:

Provided that at a joint sitting:—

(a) unless the Bill has been passed by the Legislative Council with amendments and returned to the Legislative Assembly, no amendments shall be proposed to the Bill other than such amendments, if any, as are made necessary by the delay in the passage of the Bill;

(b) if the Bill has been so passed and returned by the Legislative Council, only such amendments as aforesaid shall be proposed in the Bill and such other amendments as are relevant to the matters with respect to which the Houses have not agreed, and the decision of the person presiding as to the amendments which are admissible under this sub-section shall be final."

New clauses 146-A and 146-B.—After clause 146, insert the following clauses, namely:—

"**146-A.** ***Special provisions in respect of Money Bills.***—(1) A Money Bill shall not be introduced in a Legislative Council

(2) After a Money Bill has been passed by the Legislative Assembly of a Province having a Legislative Council it shall be transmitted to the Legislative Council for its recommendations, and the Legislative Council shall within a period of thirty days from the date of its receipt of the Bill return the Bill to the Legislative Assembly with its recommendations, and the Legislative Assembly may thereupon either accept or reject all or any of the recommendations of Legislative Council.

(3) If the Legislative Assembly accepts any of the recommendations of the Legislative Council, the Money Bill shall be deemed to have been passed by both Houses with the amendments recommended by the Legislative Council and accepted by the Legislative Assembly, and if the Legislative Assembly does not

accept any of the recommendations of the Legislative Council, it shall be deemed to have been passed by both Houses in the form in which it was passed by the Legislative Assembly without any of the Amendments recommended by the Legislative Council.

(4) If a Money Bill passed by the Legislative Assembly and transmitted to the Legislative Council for its recommendations is not returned to the Legislative Assembly within the said period of thirty days, it shall be deemed to have been passed by both Houses at the expiration of the said period of thirty days in the form in which it was passed by the Legislative Assembly.

146-B. Definition of "Money Bill".—(1) For the purposes of this Chapter, a Bill shall be deemed to be a money Bill if it makes provision—

(a) for imposing or increasing any tax; or

(b) for regulating the borrowing of money or the giving of any guarantee by the Province or for amending the law with respect to any financial obligations undertaken or to be undertaken by the Province; or

(c) for declaring any expenditure to be expenditure charged on the revenues of the Province, or for increasing the amount of any such expenditure.

(2) A Bill shall not be deemed to be a Money Bill by reason only that it provides for the imposition of fines or other pecuniary penalties or for the demand or payment of fees for licences or fees for services rendered or by reason that it provides for the imposition or increase of any tax by any local authority or body for local purposes.

(3) If any question arises whether a Bill is a Money Bill or not, the decision of the Speaker of the Legislative Assembly thereon shall be final.

(4) There shall be endorsed on every Money Bill when it is transmitted to the Legislative Council under section 146-A after it has been passed by the Legislative Assembly, and when it is presented to the Governor for assent under section 147, the certificate of the Speaker of the Legislative Assembly signed by him that it is a Money Bill."

Clause 148.—In the proviso to clause 148, after the words "Provided that" *insert* the words "if the Bill is not a Money Bill"

Clause 151.—In sub-clause (3) of clause 151, for the words "succeeding section" *substitute* the words "two succeeding sections".

New Clause 152-A.—After clause 152, *insert* the following clause namely:—

"***152-A. Excess grants.***—If in any financial year expenditure from the revenues of the Province has been incurred on any service for which the vote of the Legislative Assembly is necessary in excess of the amount granted for that service and for that year, a demand for the excess shall be presented to the Assembly and the provisions of sections 150 and 151 shall have effect in relation to such demand as they have effect in relation to a demand for a grant."

Clause 153.—For clause 153, *substitute* the following clause namely:—

"***153. Special provisions as to financial Bills.***—(1) A Money Bill or an amendment thereto shall not be introduced or moved except on the recommendation of the Governor.

(2) A Bill which if enacted and brought into operation, would involve expenditure from the revenues of a Province shall not be passed by a House of the Provincial Legislature unless the Governor has recommended to that House the consideration of the Bill."

Provisions relating to the Auditor-General of the Province.

Clause 174—For sub-clause (3) of clause 174, *substitute* the following, namely:—

"(3) The Auditor-General of a Province shall be eligible for appointment as Auditor-General of the Federation or as Auditor-General of any other Province but not for any other appointment either under the Federation or under the Government of a unit after he has ceased to hold his office."

Provisions relating to distribution of revenues between the Federation and units and miscellaneous Financial provisions.

Clause 194-A.—For clause 194-A *substitute* the following namely —

"***194-A. Interpretation.***—In this Part—

(a) 'Finance Commission' means the Finance Commission constituted under Section 202-A of this Constitution;

(b) 'unit' does not include a Chief Commissioner's Province "

Clauses 196 to 199.—For clauses 196 to 199, *substitute* the following, namely:—

"***196. Certain succession duties.***—(1) Duties in respect of succession to property other than agricultural land and estate duty in respect of property other than agricultural land shall be levied and collected by the Federation, but sixty per cent. or such higher percentage as may be prescribed of the net proceeds in any financial year of any such duty, except in so far as those proceeds represent proceeds attributable to Chief Commissioners' Provinces, shall not form part of the revenues of the Federation, but shall be assigned to the units within which that duty is leviable in that year, and shall be distributed among the units in accordance with such principles of distribution as may be prescribed.

(2) If any dispute arises as to the distribution of the net proceeds of any such duty among the units, it shall be referred for decision to such authority as may be appointed in this behalf by the President and the decision of such authority shall be final.

196-A. Certain terminal taxes.—Terminal taxes on goods or passenger carried by railway or air small be levied and collected by the Federation, but the net proceeds in any financial year of any such tax, except in so far as those proceeds represent proceeds attributable to Chief Commissioners' Provinces, shall not form part of the revenues of the Federation, but shall be assigned to the units within which that tax is leviable in that year, and shall be distributed among the units in accordance with such principles of distribution as may be prescribed.

196-B. Certain stamp duties.—Such stamp duties as are mentioned in the Federal Legislative List shall be levied by the Federation and collected, in the case where such duties are leviable within any Chief Commissioner's Province, by the Federation and in other cases, by the units within which such duties are respectively leviable, but the proceeds in any financial year of any such duty leviable in that year within any unit shall not form part of the revenues of the Federation, but shall be assigned to that unit.

197. Taxes on Income.—(1) Taxes on income other than agricultural income shall be levied and collected by the Federation, but sixty per cent., or such higher percentage as may be prescribed, of the net proceeds in any financial year of any such tax, except in so far as those proceeds represent proceeds attributable to Chief Commissioners' Provinces shall not form part of the revenues of the Federation, but shall be assigned to the units within which that tax is leviable in that year, and shall be distributed among the units in such manner as may be prescribed:

Provided that the Federal Parliament may, at any time, increase the said taxes by a surcharge for Federal purposes and the whole proceeds of any such surcharge shall form part of the revenues of the Federation.

(2) In this section, "taxes on income" includes any sum levied by the Federation in lieu of any tax on income but does not include any contributions levied by the Federation in respect of its own undertakings.

198. Salt duties and excise duties.—(1) No duties on salt shall be levied by the Federation.

(2) Federal duties of excise shall be levied and collected by the Federation, but, if an Act of the Federal Parliament so provides, there shall be paid out of the revenues of the Federation to the units to which the Act imposing the duty extends, sums equivalent to the whole or any part of the net proceeds of that duty, and those sums shall be distributed among the units in accordance with such principles of distribution as may be prescribed:

Provided that fifty per cent., or such higher percentage as may be prescribed, of the net proceeds in any financial year of the excise duty on tobacco, except in so far as those proceeds represent proceeds attributable to Chief Commissioners Provinces, shall not form part of the revenues of the Federation but shall be assigned to the units within which that duty is leviable in that year, and shall be distributed among the units in such manner as may be prescribed.

198-A. Taxes not enumerated in any of the lists in the Ninth Schedule.—If any tax not mentioned in any of the lists in the Ninth Schedule to this Constitution is imposed by Act of the Federal Parliament by virtue of entry 90 of the Federal Legislative List, such tax shall be levied and collected by the Federation but a prescribed percentage of the net proceeds in any financial year of any such tax, except in so far as those proceeds represent proceeds attributable to Chief Commissioners' Provinces, shall not form part of the revenues of the Federation, but shall be assigned to the units within which that tax is leviable in that year, and shall be distributed among the units in accordance with such principles of distribution as may be prescribed.

198-B. Grants in lieu of jute Export Duty.—Until the abolition of the export duty levied by the Federation on jute or jute products or the expiration of ten years from the commencement of this Constitution, whichever is earlier, there shall be charged on the revenues of the Federation in each year as grants-in-aid of the revenues of the Provinces mentioned below the sums respectively specified against those Provinces:

Province	*Sum*
West Bengal	100 lakhs of rupees.
Bihar	17 lakhs of rupees.
Assam	15 lakhs of rupees.
Orissa	3 lakhs of rupees.

199. Grants from Federation to certain Units.—Such sums as the President may, on the recommendation of the Finance Commission, by order fix shall be charged on the revenues of the Federation in each year as grants-in-aid of the revenues of such units as the President may on such recommendation determine to be in need of assistance, and different sums may be fixed for different units:

Provided that there shall be charged on the revenues of the Federation in each year as grants-in-aid of the revenues of the Provinces of Assam and Orissa the sums of thirty and forty lakhs of rupees respectively or such higher sums as the President may on the recommendation of the Finance Commission fix in respect of either of these Provinces:

Provided further that there shall be paid out of the revenues of the Federation as grants-in-aid of the revenues of a Province such capital and recurring sums as may be necessary to enable that Province to meet the costs of such schemes of development as may be undertaken by the Province with the approval of the Federal Government for the purpose of promoting the welfare of the scheduled tribes in the Province or raising the level of administration of the scheduled areas in the Province to that of the administration of the rest of the Province:

Provided also that there shall be paid out of the revenues of the Federation as grants-in-aid of the revenues of the Province of Assam sums, capital and recurring, equivalent to—

(a) the average excess of expenditure over the revenues during the three years immediately preceding the date of commencement of this Constitution in respect of the administration of the areas specified in Part I of the table appended to paragraph 19 of the Eighth Schedule to this Constitution; and

(b) the costs of such schemes of development as may be undertaken by that Province with the approval of the Federal Government for the purpose of raising the level of administration of the said areas to that of the administration of the rest of the Province.

Clause 200.—In sub-clause (2) of clause 200, for the word "fifty", wherever it occurs, *substitute* the words "two hundred and fifty".

New Clause 201-A.—After clause 201, *insert* the following clause, namely:—

"201-A. Application of the provisions relating to distribution of revenues during the period a Proclamation of Emergency is in operation.—Where a proclamation of Emergency is in operation whereby the President has declared that the security of India is threatened, then, notwithstanding anything contained in the foregoing provisions of this Chapter, the President may, by order, direct that all or any of those provisions shall, until the expiration of the financial year in which such Proclamation ceases to operate, have effect subject to such exceptions or modifications as may be specified in such order."

Clause 202.—For clause 202, *substitute* the following, namely:—

"202. Definition of 'prescribed' and calculation of 'net proceeds' etc.—(1) In the foregoing provisions of this Chapter—

(a) 'prescribed' means—

(i) until the Finance Commission has been constituted, prescribed by order of the President; and

(ii) after the Finance Commission has been constituted, prescribed by order of the President on the recommendation of the Finance Commission;

(b) 'net proceeds' means in relation to any tax or duty the proceeds thereof reduced by the cost of collection, and for the purposes of these provisions the net proceeds of any tax or duty, or of any part of any tax or duty, in or attributable to any area shall be ascertained and certified by the Auditor-General of the Federation, whose certificate shall be final.

(2) Subject as aforesaid, and to any other express provision in this Chapter, an order of the President may, in any case where under this Part of this Constitution the proceeds of any duty or tax are, or may be, assigned to any unit, provide for the manner in which the proceeds are to be calculated, for the time from or at which and the manner in which any payments are to be made, for the making of adjustments between one financial year and another, and for any other incidental or ancillary matters."

New Clause 202-A and 202-B.—After clause 202, *insert* the following clauses namely:—

"***202-A. Finance Commission.***—(1) There shall be a Finance Commission which shall consist of a Chairman and four other members to be appointed by the President in his discretion.

(2) The Chairman shall be a person who holds or has held judicial office not inferior in rank to that of a Judge of a High Court.

(3) The members of the Commission shall receive such remuneration as the President may by order determine and shall hold office for a term of five years and may on the expiry of such term be re-appointed for another term of five years.

(4) It shall be the duty of the Commission to perform the functions conferred on the Commission by this Chapter or by any other law for the time being in force and to give advice to the Federal Government upon such financial matters or to perform such other duties of a financial character as may from time to time be referred or assigned to it by the President.

(5) The Commission shall determine its procedure and shall have such powers in the performance of its functions as the President may by order confer on it.

202-B. Recommendations of the Finance Commission.—The President shall cause every recommendation made by the Finance Commission under the foregoing provisions of this Chapter together with an explanatory memorandum, as to the action taken thereon by the President to be laid before the Federal Parliament."

Clause 207.—To clause 207, *add* the following Explanation, namely:—

"***Explanation.***—For the purposes of this section, any undertaking by the Government of any unit, such as the sale of the forest produce of any forest under the control of such unit or of any article produced in any jail within such unit, shall not be deemed to be a trade or business carried on by or on behalf of such Government."

Provisions relating to borrowing

Clause 210.—In sub-clause (3) of clause 210, for the word "Province", in the two places where it occurs, *substitute* the word "unit"

Ninth Schedule

Provincial Legislative Lists.

In the Provincial Legislative List in the Ninth Schedule—

(1) in entry 48, *omit* the words "hearths and windows";

(2) for entry 50, *substitute* the following, namely:—

"50 Taxes on the sale, turnover or purchase of goods including taxes in lieu thereof on the use or consumption within the Province of goods liable to taxes within the Province on sale, turnover or purchase; taxes on advertisement;"

(3) in entry 53, for the word "Cesses" *substitute* the word "Taxes"; and

(4) in entry 56, for the word "Does" *substitute* the word "Taxes".

GIPD—S2—141CA—16-1-43—150.